



## ERGO

*Analysing developments impacting business*

### GOVERNMENT WALKS THE TALK; ABU DHABI'S SOVEREIGN WEALTH FUND BECOMES THE FIRST FUND TO GET TAX EXEMPTION FOR INFRA INVESTMENTS, ADDITIONAL CONDITIONS PRESCRIBED!

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MIC Redwood 1 RSC Limited, Abu Dhabi, United Arab Emirates (Fund) was recently conferred the tax exemption intended for a sovereign wealth fund (SWF) under the Income-tax Act, 1961 (Tax Act).

#### What is the tax exemption?

Dividends, interest and long-term capital gains earned by SWFs and Pension Funds from investments in specified "infrastructure business" are sought to be completely exempt.

The exemption seeks to incentivise investment in diverse sectors. "Infrastructure business" for the purposes of the exemption would include sectors like transport, energy, water, sanitation, telecommunication, and "social and commercial infrastructure". "Social and commercial infrastructure" in turn includes hospitals, tourism, education institutions, affordable housing, and the likes. For a comprehensive list, please click [here](#).

#### What are the key statutory conditions to qualify for the exemption?

- The investment can be in the form of share capital, debt or units in an InvIT or an entity engaged in "infrastructure business" (including investments routed through an Alternative Investment Fund (Category I or II) having 100% investment in such entity).
- The investment is made between 1 April 2020 to 31 March 2024. So long as the investment is made within the stipulated period, the income would continue to be exempt till the time such investment is held. Further, such investment should be held for a period of at least 3 years.
- SWF must be wholly owned and controlled, directly or indirectly, by the government of the foreign country. In addition, there are strict conditions to ensure the SWF does not engage in any commercial activity in or outside India and the income of the SWF would at all times be beneficially owned by the respective government, including at the time of winding up.

#### Is the exemption automatic?

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No, the exemption would only be available on a specific approval from the Central Government and is not automatic even if the stipulated conditions are met.

The Central Government has the power to prescribe additional conditions, in addition to the statutory conditions, at the time of the grant of approval that could be case specific.

## Additional conditions prescribed for the Fund - would they set a precedent?

- Fund to not have any private investment: The Fund should not have any loan, borrowing, advances, deposits, or investment in it of any kind, directly or indirectly, from any person other than the Government of Abu Dhabi.
- Fund to not have any borrowings: The Fund shall only invest the surplus fund of the Government of Abu Dhabi and the Government shall not have raised any debt, directly or indirectly, from the market or any entity.
- Restrictions on controlling rights / interest: The Fund can adopt a monitoring mechanism to protect the investment with investee but shall not i) manage the day to day operations of the investee or ii) appoint executive directors in the investee company or iii) participate in the decision making process.
- Prospective exemption: The exemption would only cover investments made post the date of the exemption notification and is not retrospective for the entire financial year of the application.

Given the nature of additional conditions which seek to ensure the money being invested is indeed self-generated income of the foreign government, such conditions are likely to be placed on subsequent grants as well.

## Concluding thoughts

The impact of restrictions on having controlling rights or ability to appoint executive directors in the investee company may need to be analysed more closely. Such restrictions certainly raise the question of whether they could be a deterrent to attracting investments directly in private entities. Such aspects should be kept in mind by other SWFs seeking the exemption and whether the conditions could be relaxed to ensure control in cases of majority shareholding.

Having said that, the Fund's application for exemption seems to have been processed and approved expeditiously ie, in less than 2 months as per media reports. The efficacious handling of the process will only encourage more applicants.

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