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TO

VERRA

LEGAL OPINION ON TRANSFER OF CARBON RIGHTS

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I. BACKGROUND

1.1. JSW Hydro Energy Limited ("**JSW Hydro**") (formerly known as Himachal Baspa Power Company Limited ("**HBPCL**") inter alia owns and operates two hydropower plants - 300 megawatts (MW) Baspa II ("**Project I**") and 1,000 MW Karcham Wangtoo ("**Project II**"), located in Himachal Pradesh. Project I and Project II are hereinafter collectively referred to as "**Projects**".

1.2. We have been provided with the details of the transfer of ownership of Project I, since its inception and have set out our understanding of the facts below:

a. **1992:** Implementation Agreement dated October 1, 1992 executed between Jaiprakash Industries Limited ("**JIL**") and the Government of Himachal Pradesh ("**HP Govt**") ("**Implementation Agreement**") where the HP Govt granted JIL the right to establish, own, operate and maintain Project I and also generate and sell power from Project I.

b. **1995:** Tripartite agreement dated October 1, 1995 executed amongst HP Govt, JIL, and Jaiprakash Hydro Power Limited ("**JHPL**") (a subsidiary of JIL) ("**1995 Tripartite Agreement**"). By way of this 1995 Tripartite Agreement, JIL transferred and assigned to JHPL (later known as JPVL) and JHPL (later known as JPVL) agreed to take over all the assets, liabilities, obligations, rights, ***privileges and benefits*** of Project I accruing to JIL by way of the Implementation Agreement and other related documents.

c. **2009:** JHPL changed its name to Jaiprakash Power Ventures Limited ("**JPVL**") on December 23, 2009.

d. **2015:** All assets, obligations, liabilities, rights, ***privileges and benefits*** of Project I were transferred from JPVL to Himachal Baspa Power Company Limited ("**HBPCL"**) by way of a demerger scheme approved by the High Court of Himachal Pradesh on June 25, 2015 ("**Demerger Scheme**").

It is pertinent to note that Schedule I (Description of Undertaking) annexed to the Demerger Scheme and relating to Project I includes, *inter alia*, "*….any other assets, property or rights of the Transferor Company in respect of the Transferred Undertaking No. 1 including but not limited to powers, authorities, permits, allotments, approvals, consents,* ***privileges,*** *liberties, advantages, easements and all the rights, titles, interests, benefit and advantage (including tax benefits and tax holidays including but not limited to section 80A benefit), grants, subsidies, concessions, deposits, reserves, provisions, advances, receivables, funds, accounts and all other rights, claims and ownership of whatsoever nature and wherever situated belonging or in possession of or granted in favour of or enjoyed by the Transferor Company (i.e. JPVL) in connection with or pertaining or relatable to the business of the Transferred Undertaking No. 1 (i.e. Project I)*".

More particularly, we note that the said schedule includes '*The Certified Emission Reductions and Verified Emission Reductions accrued for the period prior to the Effective Date in relation to the Transferred Undertaking No. 1"* as part of the transferred assets.

e. **2015:** On August 29, 2015, another tripartite agreement was entered into between the HP Govt., JPVL and HBPCL ("**2015 Tripartite Agreement"**) where the HP Govt granted its consent to transfer / assign all assets, liabilities, obligations, ***privileges,*** *no objection certificates*, ***benefits,*** accruing to JPVL arising out of the Implementation Agreement and the 1995 Tripartite Agreement. Further, JPVL was also released of all of its obligations under the said agreements by the HP Govt. We also understand that JSW Energy Limited acquired the securities of HBPCL during this period.

f. **2018:** HBPCL changed its name to JSW Hydro on September 11, 2018.

1.3. Verra is the Verra Registry administrator in relation to Project I. As part of registration and issuance process followed by Verra, a 'Project Proponent' (i.e., the individual or organization that has overall control and responsibility for the project, whether individually or together with others, and can demonstrate project ownership in respect of the project) is required to submit certain documents, including a Registration Deed of Representation ("**Registration Deed**"). Under this deed, *inter alia*, a representation is made by the Project Proponent which states that, "*Registration Representors collectively hold full and exclusive legal and equitable title and rights to all and any Reductions generated by the Project for which the Registration Representors are eligible to request VCU issuance…*".

1.4. Where there is a change in ownership of the project, Verra requires the existing and incoming Project Proponents to provide a Deed of Accession in respect of the Registration Deed, along with a Deed of Partial Release. As part of the Deed of Accession, the existing Project Proponent acknowledges and agrees to the accession of the incoming Project Proponent, and the incoming Project Proponent agrees to be bound by the representations made by the existing Project Proponent under the registration deed. Under the Deed of Partial Release, Verra agrees to release the existing Project Proponent from the representations that the existing Project Proponent had made in the Registration Deed.

1.5. In the present case, we understand that JPVL's signatures to the Deed of Accession and Deed of Partial Release required in relation to Project I have not been obtained. However, Verra may waive the need to obtain JPVL's signatures to the Deed of Accession and Deed of Partial Release if it is satisfied that JSW Hydro has all full and exclusive legal and equitable rights to the carbon credits achieved by Project I. In light of the facts above, Verra has raised the queries set out in Part 2 below, as part of the letter of instruction provided to us.

II. QUERIES

2.1. Under Indian law, in respect of Project I, are carbon rights defined as a separate right, or are carbon rights linked to the Implementation Agreement and / or the 2015 Tripartite Agreement?

a. Where carbon rights are not defined as a separate right, do carbon rights automatically transfer along with any transference of the rights referred to in the Implementation Agreement and / or the 2015 Tripartite Agreement?

b. Where carbon rights are defined as a separate right, do carbon rights automatically transfer along with any transference of the rights referred to in the Implementation Agreement and / or the 2015 Tripartite Agreement?

c. Where carbon rights do not automatically transfer along with the transference of the rights referred to in the Implementation Agreement and / or the 2015 Tripartite Agreement, what are the formalities required for the transfer of the carbon rights?

2.2. Where the Hydro Project is defined in the Implementation Agreement as "Baspa Hydro Electric Project Stage-II of 300MW capacity as may be finally approved by the General Electricity Authority, including the transmission system up to Jhakri Sub Station of Nachpa Johari Project for evacuation of power from the Project", as a matter of Indian law, would this include the carbon rights that are transferred?

2.3. Based on the 2015 Tripartite Agreement, it states that an Agreement had been signed between the First Party (Government of Himachal Pradesh) and JHPL whereby "all assets, obligations, liabilities, rights, privileges and benefits of the Project were transferred to JHPL".

a. Under Indian law, does "all assets, obligations, liabilities, rights, privileges and benefits" include carbon rights, in the event where carbon rights are not defined as a separate right associated with the transferred rights?

b. Under Indian law, does "all assets, obligations, liabilities, rights, privileges and benefits" include carbon rights, in the event where carbon rights are defined as a separate right associated with the transferred rights?

III. LEGAL PROVISIONS

3.1. Under Indian law, 'carbon rights' are not defined statutorily and there is no legislation that governs the transfer of such carbon rights. However, to understand these rights and their treatment under Indian law, we rely on precedents under the Income Tax Act, 1961 ("**IT Act**") where taxability of the income derived from trading of carbon rights has been adjudicated upon by the courts. Certain key observations made by the courts / tribunals in this regard have been set out below:

3.2. The High Court of Karnataka discussed the nature of carbon rights in Commissioner of Income Tax-III vs. Subhash Kabini Power Corporation Limited[1] and stated:

"*Carbon credit is in the nature of "an entitlement" received to improve world atmosphere and environment reducing carbon, heat and gas emissions.*

The entitlement earned for carbon credits can, at best, be regarded as a capital receipt and cannot be taxed as a revenue receipt. It is not generated or created due to carrying on business but it is accrued due to "world concern". It has been made available assuming character of transferable right or entitlement only due to world concern.

The source of carbon credit is world concern and environment. Due to that the assessee gets ***a privilege in the nature of transfer of carbon credits****. .... Carbon credits are made available to the assessee on account of saving of energy consumption and not because of its business. Further, in our opinion, carbon credits cannot be considered as a bi-product. It is a credit given to the assessee under the Kyoto Protocol and because of international understanding. Thus, the assessees who have surplus carbon credits can sell them to other assesses to have capped emission commitment under the Kyoto Protocol. Transferable carbon credit is not a result or incidence of one's business and it is a credit for reducing emissions. The persons having carbon credits get benefit by selling the same to a person who needs carbon credits to overcome one's negative point carbon credit. The amount received is not received for producing and/or selling any product, bi-product or for rendering any service for carrying on the business.* ***In our opinion, carbon credit is entitlement or accretion of capital and hence income earned on sale***

[1] (2016) 287 CTR (Kar) 147

of these credits is capital receipt*. ….. Carbon credit is not an offshoot of business but an offshoot of environmental concerns. No asset is generated in the course of business but it is generated due to environmental concerns. Credit for reducing carbon emission or greenhouse effect can be transferred to another party in need of reduction of carbon emission. It does not increase profit in any manner and does not need any expenses. It is a nature of entitlement to reduce carbon emission, however, there is no cost of acquisition or cost of production to get this entitlement. Carbon credit is not in the nature of profit or in the nature of income.*

Further, as per guidance note on accounting for Self-generated Certified Emission Reductions (CERs) issued by the Institute of Chartered Accountants of India (ICAI) in June, 2009 states that CERs should be recognised in books when those are created by UNFCCC and/or unconditionally available to the generating entity. CERs are inventories of the generating entities as they are generated and held for the purpose of sale in ordinary course. Even though CERs are intangible assets those should be accounted as per AS-2 (Valuation of inventories) at a cost or market price, whichever is lower. Since CERs are recognised as inventories, the generating assessee should apply AS-9 to recognise revenue in respect of sale of CERs."

3.3. In M/s. My Home Power Ltd. Hyderabad vs. Dy. CIT Central Circle-7, Hyderabad,[2] ITAT, Hyderabad bench dealing with the issue, had observed that;

"*The source of carbon credit is the world concern and environment. The assessee was given a* ***privilege*** *in the nature of carbon credit. Therefore, there is no element of profit or gain; hence it cannot be subject-matter of taxation. Carbon credit cannot also be considered by a byproduct. It is a credit given to the assessee under the Kyoto Protocol. The amount received by the assessee is not for producing or selling any byproduct or rendering any services. The carbon credit is an entitlement or accretion of the capital asset. Therefore, the income earned on sale of these credits is a capital receipt.*"[3]

3.4. Subsequently, the Andhra Pradesh High Court in CIT vs. My Home Power Limited[4] confirmed the above ruling of ITAT, Hyderabad and stated that "*…as the learned Tribunal has factually found that 'carbon credit is not an offshoot of business but an offshoot of environmental concerns. No asset is generated in the course of business but it is generated due to environmental concerns. The Carbon Credit is not even directly linked with power generation. We agree with the factual analysis as the assessee is carrying on the business of power generation.*"

IV. ANALYSIS

4.1. In light of the background set out above and the legal interpretation we note that:

a. whilst the Implementation Agreement, the 1995 Tripartite Agreement and the 2015 Tripartite Agreement do not specifically refer to the 'carbon rights', they relate to grant of ownership of Project I as well transfer of all assets, liability, obligations, rights, ***privileges*** and benefits relating to the Project.

b. the Demerger Scheme – which is approved by the court has JPVL as party to it, and specifically includes '*The Certified Emission Reductions and Verified Emission Reductions accrued for the period prior to the Effective Date in relation to the Transferred undertaking No. 1*' as part of the transferred assets. It is pertinent to note that the change in the 'owner' of Project I took place through a share purchase by JSW

[2] 2013 (21) ITR(Trib) 186 (Hyderabad)
[3] [2013] 21 ITR (Trib) 186 (Hyderabad)
[4] ([2014] 365 ITR 82 (AP))

Energy Limited of HBPCL (later known as JSW Hydro) (after the Demerger Scheme became effective). Subsequently, the name of HBPCL was changed to JSW Hydro.

4.2. From a reading of the above, we note that the carbon rights would stand transferred as a part of the Demerger Scheme from JPVL to HBPCL (which later changed its name to JSW Hydro). Accordingly, the ownership of the carbon rights achieved by Project I vests with JSW Hydro, by the express inclusion of these rights in the Demerger Scheme.

4.3. In addition, under Indian law, the accrual of carbon rights is not separately legislated. We note that the Implementation Agreement and the 1995 Tripartite Agreement do not state anything to the contrary in terms of the accrual of the carbon rights.

4.4. In light of :

a. the precedents set out above, which state that *'the Carbon Credit is not even directly linked with power generation'* and is a by product of the business activity; and

b. the fact that the Implementation Agreement and the 1995 Tripartite Agreement do not state anything to the contrary in terms of the accrual of the carbon rights;

in our view, the carbon rights from Project I belong to the project developer (in this case JPVL and subsequently JSW Hydro).

5. RESPONSES TO QUERIES

5.1. Our responses to the queries are as under:

a. Under Indian law, in respect of Project I, are carbon rights defined as a separate right, or are carbon rights linked to the Implementation Agreement and / or the 2015 Tripartite Agreement?

(i) *Where carbon rights are not defined as a separate right, do carbon rights automatically transfer along with any transference of the rights referred to in the Implementation Agreement and / or the 2015 Tripartite Agreement?*

(ii) *Where carbon rights are defined as a separate right, do carbon rights automatically transfer along with any transference of the rights referred to in the Implementation Agreement and / or the 2015 Tripartite Agreement?*

(iii) *Where carbon rights do not automatically transfer along with the transference of the rights referred to in the Implementation Agreement and / or the 2015 Tripartite Agreement, what are the formalities required for the transfer of the carbon rights?*

Response: As noted above, carbon rights are not defined as a separate right under the Indian law. Whilst the Implementation Agreement and the 2015 Tripartite Agreement do not specifically refer to the 'carbon rights', they relate to grant of ownership of Project I as well transfer of all assets, liability, obligations, rights, ***privileges* and benefits** relating to the Project. Given that carbon rights are 'privileges' in light of the precedents quoted above, in our view, they form part of the transfers under the aforementioned agreements.

Under Clause 4.1 of the Demerger Scheme, the entire Project shall be transferred to, vested in or be deemed to have been transferred to and vested in the transferee company (i.e. JSW Hydro) on a going concern basis. Clause 4.2 of the Scheme of Demerger further notes that, without prejudice to the generality of the Clause 4.1, all the assets and properties forming part of Project I shall be transferred and stand vested in the transferee entity.

Therefore, there is no further action or deed required to be undertaken to transfer the assets to the transferee company.

b. *Where the Hydro Project is defined in the Implementation Agreement as "Baspa Hydro Electric Project Stage-II of 300MW capacity as may be finally approved by the General Electricity Authority, including the transmission system up to Jhakri Sub Station of Nachpa Johari Project for evacuation of power from the Project", as a matter of Indian law, would this include the carbon rights that are transferred?*

Response: Please refer to our response in a. above.

c. *Based on the 2015 Tripartite Agreement, it states that an Agreement had been signed between the First Party (Government of Himachal Pradesh) and JHPL whereby "all assets, obligations, liabilities, rights, privileges and benefits of the Project were transferred to JHPL".*

(i) *Under Indian law, does "all assets, obligations, liabilities, rights, privileges and benefits" include carbon rights, in the event where carbon rights are not defined as a separate right associated with the transferred rights?*

(ii) *Under Indian law, does "all assets, obligations, liabilities, rights, privileges and benefits" include carbon rights, in the event where carbon rights are defined as a separate right associated with the transferred rights?*

Response: As noted above, carbon rights are not defined as a separate right under the Indian law. Whilst the Implementation Agreement and the 2015 Tripartite Agreement do not specifically refer to the 'carbon rights', they relate to grant of ownership of Project I as well transfer of all assets, liability, obligations, rights, ***privileges* and benefits** relating to the Project. Given that carbon rights are 'privileges' in light of the precedents quoted above, in our view, they form part of the transfers under the aforementioned agreements.

Yours truly,

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BASIS AND SCOPE OF THE OPINION

1. This legal opinion is addressed to Verra solely for their benefit. We understand from Verra that this opinion will be shared with JSW Hydro Energy Limited, which will be subject to, at all times, the basis and scope of the memorandum as set out hereunder. Except for Verra, this legal opinion shall not be distributed, referred to or quoted, in whole or in part, without our prior written consent, except that the legal opinion can be shared with Verra's legal counsel (advisors to Verra on a non-reliance basis). This legal opinion is not to be transmitted to anyone else nor is to be relied upon by anyone else or for any other purpose or quoted or referred to in any public document or filed with any person or authority without our express written consent.

2. This legal opinion is based on Indian law in force as of the date of its issue, without consideration of the applicable conflict of law principles, and we do not pass upon nor express any opinion in respect to those matters governed by or construed in accordance with the laws of any jurisdiction other than the Republic of India.

3. A certificate, determination, notification, memorandum or the like will not be binding on an Indian court or any arbitrator or judicial or regulatory body which would have to be independently satisfied, despite any provision in the documents to the contrary.

4. The possibility that a court of law or other authority in India may take a view contrary to that of ours as expressed herein cannot be ruled out.

5. We have not analysed the provisions of laws relating to winding up, liquidation, insolvency, or similar laws of general application such as the Insolvency and Bankruptcy Code, 2016, since we understand from the publicly available information that the Companies are not facing any proceedings under such laws.