KATALYST
ADVISORS PVT. LTD.

# Katalyst Kaleidoscope

December 2021: Tax and Regulatory Insights

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## A. Income Tax highlights

### 1. Mumbai ITAT: Gift of brand 'Essar' to corpus of private irrevocable trust, non-taxable receipt[1]

Balaji Trust (the Assessee), a private and irrevocable discretionary trust, was settled on March 29, 2012 by Shri Shashikant Ruia for the benefit of the members of the Ruia Family. Essar Investments Limited (EIL) voluntarily gifted the 'Essar' brand to the Trust on March 29, 2012 without any consideration. The Trust entered into brand licensing agreements with Essar group entities and granted a non-exclusive license to use the Brand in India for license fees which was accounted as income in FY 2012-13 and onwards, under the cash system of accounting.

The Assessing Officer (AO) held that the definition of 'income' u/s 2(24) of the Income tax Act, 1961 (the Act), which provides inclusive definition of "income", was wide enough to include the receipt of trademark and copyright. Therefore, the AO taxed the transaction under the head Income from Other Sources u/s 56(1), [which provides for taxation of notional income on receipt (as a gift) of certain 'property']. The AO also considered that the brand received could be taxed u/s 28(iv) of the Act, which taxes the value of any benefit or perquisite arising from the business or exercise of profession.

On first appeal the CIT(A) held that the receipt of Brand was a capital receipt and in any case, the definition of 'property' u/s 56(2) did not include the Brand, because a brand is not a 'work of art'; and in so far as the AO stand regarding it being business income is concerned, that question does not arise, since the Trust was not carrying on any business when it received the Brand.

The ITAT observed the following:

- the brand, which was transferred to the Trust, did not carry any value in the books of Essar India Limited;
- the Assessee received the Brand as a gift, and it would be a capital receipt because it constituted the Trust's profit making apparatus;
- the brand neither carried any element of profit, nor fell under any category of income specified under Sections 2(24) and Section 56 of the Act, and its potential to generate royalty income could be realised only when the group companies were willing to pay and

[1] Balaji Trust [TS-1092-ITAT-2021(Mum)] on November 25, 2021

not otherwise, therefore, the contribution of the Brand as a gift by EIL to the corpus of the Trust would not fall under any category of income;

- the argument of CIT(A) with regard to the Brand being registered as an 'artistic work' under the Copyrights Act, 1957 and therefore, would fall in the definition of 'property' under Explanation (d) to Section 56(2)(vii)(c) was not correct, as 'artistic work' used under the Copyright Act was meant to protect the rights of an artist which was different from the purpose with which 'any work of art' used u/s 56(2)(vii). The Mumbai ITAT held that the brand Is not a 'work of art' and therefore, does not fall within the definition of 'property' and therefore, Section 56(2) does not apply to the gift, even on this count.

The Mumbai ITAT therefore dismissed Revenue's appeal and held that gifting of brand 'Essar' by a unanimous resolution by Essar India Limited to an irrevocable trust on the date of its settlement was not a taxable event.

***Katalyst Comments:***

*This is an interesting decision from various angles; one is that it acknowledges and endorses the concept of a corporate gift, and secondly, it reiterates the principle that a profit making apparatus which can generate income is itself not income, but a capital receipt.*

## 2. Tax holiday deduction under section 80IA available on amalgamation[2]

The facts of the matter before the Mumbai ITAT were that Ultratech Cement ('Ultratech') is a subsidiary of Grasim Industries; Ultratech entered into the scheme of amalgamation with its co-subsidiary Samruddhi Cements Ltd ('SCL'), whereby SCL was amalgamated with the assessee with effect from July 1, 2010; Ultratech claimed a deduction under section 80IA in relation to two undertakings belonging to the erstwhile SCL. The claim was rejected by the Revenue Department and CIT(A) on the basis of Section 80-IA(12A).

Section 80-IA(12A) is an enabling provision for the amalgamated company to claim the deduction for the balance period of the deduction; however, with effect from AY 2008-2009, Section 80-IA(12A) was inserted and provided that Section 80-IA(12) shall not apply to an undertaking transferred in a scheme of amalgamation or demerger on or after April 1, 2007.

In the above context, the Tribunal held that Section 80-IA(12A) simply states that the deduction shall not apply to undertakings transferred in a scheme of amalgamation and the insertion of Section 80-IA(12A) negated the impact of sub section (12). The ITAT further observed that the CBDT Circular No. 3/2008 dated March 12, 2008 relied upon by the Revenue

[2] Ultratech Cement Ltd [TS-1133-ITAT-2021 (Mum)] December 22, 2021

tried to clarify something which is nowhere in the language of the Act nor the explanatory Memorandum. In this context, the claim of Ultratech was allowed.

### 3. Constitutional validity of AAR's abolition and BAR's constitution before Delhi HC[3] challenged

Delhi HC issued notice to the Union of India and Revenue on writ petition filed by Mother Dairy Fruits & Vegetables Pvt. Ltd., along with the Regents of the University of Michigan and Internet Fund II Pte Ltd, challenging the constitutional validity of the provisions governing abolition of Authority for Advance Rulings (AAR) and constitution of Board of Advance Rulings (BAR). The writ petition challenged the provisions of Sections 245Q(4), 245-OB(2) and 245S(3) of the Act, where the Assessee questioned the amendments made by the Finance Act, 2021 with effect from April 1, 2021 on the grounds of manifest arbitrariness and unreasonableness as there is no independent person on the Board of Advance Rulings and no tax certainty due to non-binding nature of the rulings.

***Katalyst Comments:***

(i) *Pursuant to Finance Act 2021, the AAR was substituted by the BAR with an intent to fill the gap created by the non-availability of requisite members to constitute the bench of AAR, and therefore hampering the functioning of AAR, leading to piling pending cases. BAR was brought in as an alternative for providing advance rulings, which would constitute two members, each being an officer not below the rank of Chief Commissioner. Provisions were introduced to ensure advance rulings of the BAR would not be binding on the applicant or the Department and if aggrieved, the applicant or the Department could appeal against the ruling or order passed by the Board before the High Court. However, the aforementioned criteria of constitution of BAR, only constituting the members from the tax department and non-binding nature of rulings of BAR would plug the essence of existence of advance rulings.*

*(ii) It is unfortunate that prevention and dispute resolution seem to be low on the Governments priority and the unbridled litigation is not only a cause for concern, but is completely contrary to Ease of Doing Business.*

[3] Source based information

### 4. Delhi ITAT: Expenditure on promotion of brand 'Snapdeal' allowable, revenue in nature[4]

Jasper Infotech Pvt. Ltd., Assessee Company, claimed expenditure incurred on advertisement, publicity and business promotion of INR 58.91 Cr in FY 2011-12 as business expenditure. The AO disallowed the said expenditure to the extent of 50% and held it to have been incurred for acquisition of intangible assets i.e., building of marketing network in India which had enduring benefit and therefore, capital in nature.

ITAT observed that there was neither any provision in the Act nor any material on record to suggest the fact that the assessee could not claim these expenses as revenue expenditure. ITAT further opined that the Assessee, operating in online marketing business as an aggregator, had to stay ahead of its competition and thus, engage itself in brand promotional activities and had necessity to incur these expenses. ITAT stated that the AO, having accepted the fact that the assessee could spend amounts for these activities to the extent of 50% as revenue expenditure, could not have held that 50% of such expenses are capital in nature, in the absence of any contrary evidence. ITAT pointed out that no evidence was placed on record to show that assessee had created any intangible asset, accordingly held that the expenditure incurred by the assessee were purely revenue in nature and could not be considered as capital expenditure.

***Katalyst Comments:***

*This issue has been a subject matter of litigation for years. This order would add to the plethora of pronouncements on this subject of capital vs revenue expense. Given the growth of new age clients and the huge amount of spending on brands and advertising, this Tribunal order has an important relevance.*

### 5. Delhi ITAT: Faber Castell not liable to tax on royalty accrued & waived off, backed by RBI's no-objection[5]

Faber Castell Aktiengesellschaft (Assessee Company), a tax resident of Germany (FC Germany), was entitled to royalty and interest from A.W. Faber Castell (India) Pvt. Ltd. (FC India) for use of its trademark and offered royalty of INR 2.36 Cr and interest of INR 23.84 Lacs to tax, for FY 2013-14 in accordance with the India-Germany DTAA. During the assessment proceedings by the AO, Assessee, which adopted the cash basis of accounting, submitted that royalty amount was not received from FC India and the same was inadvertently offered to tax. Assessee further submitted that since FC India was facing liquidity crisis, royalty for FYs 2011-12 to 2015-16 was waived off under a termination agreement. The AO disagreed with the back-dated termination agreement and observed that FC India had already made use of the trademark/ brand name and held the royalty to be taxable.

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[4] Jasper Infotech Pvt. Ltd [TS-1111-ITAT-2021(DEL)] dated November 10, 2021

[5] Faber Castell Aktiengesellschaft Numberger [TS-1112-ITAT-2021(DEL)] on December 9, 2021

ITAT observed that FC India was facing liquidity issues and thus, payment of royalty was waived off by the Assessee. It also observed that Revenue's contention that waiver of royalty was merely an arrangement of convenience between the parties was not acceptable, as the same was backed by a 'no objection' from RBI under FEMA and noted that in view of the waiver, Assessee did not receive any royalty from FC India. ITAT relied on the co-ordinate bench rulings of Pizza Hut, Bombay HC ruling in Siemens and co-ordinate bench ruling of CSC Technologies, wherein on similar issue, it was held that "the amount which has accrued as income to a foreign company cannot be taxed in the source country, being India in this case, unless the amount has been received by the foreign company".

### 6. Bangalore ITAT: Allowed irrecoverable advance as business loss since assessee took measure under Negotiable Instruments Act, 1881[6]

Foretell Business Solutions Pvt. Ltd., the Assessee Company, was engaged in agri-business and commodity research and also served its clients by way of organising conferences etc., providing information and data services and trade/ procurement advisory. Assessee Company, with an intention to conduct a seminar at Dubai, made advance payments to Golden Gate towards booking conference hall, arrangements for lodging and boarding of guests to the Palm for the event. However, Golden Gate failed to make onward payments to the Palm Hotel. To safeguard the business interest, reputation and credibility with overseas clients, Assessee made the payments again to Golden Gate. After the event, the Assessee took steps to recover the amount from Golden Gate, and obtained post-dated cheques which remained unhonoured. Assessee also issued a legal notice and filed criminal complaint, however, with the name of the company struck off the list of companies, and the directors absconding, Assessee had to write-off the advance. The amount of loss claimed by the Assessee, being INR 1.47 Cr, was disallowed by the AO.

ITAT, in appeal, found that the Assessee had proceeded u/s 138 of the Negotiable Instruments Act, 1881, against the director of Golden Gate and also that partial payment was made to the Assessee by the entity. The AO failed to evaluate the claim as a trading loss u/s 28 of the Act. ITAT also noted the efforts of the Assessee towards recovery of the amount and relied on the Madras HC ruling in Devi Films to remark that it was incorrect to state that no legal steps were taken by the Assessee for recovery. ITAT held that there was no dispute that the advances were given in the normal course of business and that a loss arising on non-recovery of the amount was a business loss. Therefore, the ITAT allowed the Assessee's appeal, and the claim for irrecoverable advance paid in the course of business as trading loss.

[6] Foretell Business Solutions Pvt. Ltd [TS-1122-ITAT-2021(Bang)] dated November 30, 2021

***Katalyst Comments:***

*This is an important order in the context of the fact that it lays down the principle that an advance given and written off can also be allowed as a deduction, on facts.*

### 7. Canadian Supreme Court decides GAAR controversy over capital gains exemption in Alta Energy's favour[7]

The taxpayer, a Luxembourg company, was owned by a limited partnership. The members of the limited partnership were generally not Luxembourg residents. The taxpayer held shares in a Canadian company, which, in turn, held interest in Canadian resource properties (oil and gas leases in Alberta), in which it carried on exploration and production activities. When the taxpayer sold the shares of Canadian Company in 2013, it realized a capital gain of more than $380 million and claimed exemption from tax in Canada. The taxpayer claimed exemption under Article 13(4)(a) of the DTAA between Canada and Luxembourg (the Treaty), which entitles Canada to tax a resident of Luxembourg on gains arising from the alienation of shares if the value of such shares is derived principally from immovable property situated in Canada. The term "immovable property" expressly excludes property through which the business of the corporation is carried on.

The Tax Court of Canada (TCC) and the Federal Court of Appeal (FCA) found that the taxpayer qualified for an exemption under the Treaty. It also found that the transaction was not taxable as the underlying assets were property in which the business of the corporation was carried on under Article 13(4)(a) and that the GAAR did not apply to deny the resulting Treaty benefit.

Supreme Court of Canada upheld the ruling of Federal Court of Appeal on capital gains exemption in respect of sale of shares of its Canadian subsidiary, holding that:

- the Revenue's arguments that treaty shopping is inherently abusive and there are additional requirements not grounded in the text of the Canada-Luxembourg DTAA are incorrect since it effectively allows Canada to "revisit its bargain" with Luxembourg;
- the Duke of Westminster principle that the taxpayers are entitled to arrange their affairs to minimize the amount of tax payable is affirmed and the unbridled application of Duke of Westminster principle is not correct;
- treaty shopping becomes abusive where taxing rights are allocated on the basis of economic allegiance and conduit entities claim tax benefits despite the absence of any genuine economic connection with the state of residence;
- it's a two-step process for examining whether there was abuse of Article 13(4) of the DTAA: (i) identifying the object, spirit, and purpose of the provisions giving rise to the tax benefit and (ii) determining whether the transactions resulted in an abuse of these

[7] Canada v. Alta Energy Luxembourg S.A.R.L., 2021 SCC 49 dated November 26, 2021

provisions. Since the Taxpayer did not 'abuse' the provisions of Article 13(4) of the DTAA for claiming capital gains exemption, GAAR provisions would not be invoked.

***Katalyst Comments:***

*(i) The rationale provided by the Supreme Court of Canada contains useful guidance on the applicability of GAAR and the manner it might apply to other tax disputes involving a tax treaty. However, future cases arising from tax treaties pursuant to MLI, and in particular the principal purpose test (PPT) need to be considered.*
*(ii) An important principle that the judgement has reiterated is that tax payers are entitled to arrange their affairs to minimize the amount of tax payable, so long as the transaction itself is commercially justifiable.*

### 8. MoS Finance: Undisclosed credits of INR 20,353 Crores detected, with respect to 930 India linked entities in Panama and Paradise Paper leaks[8]

In a press release by the Union Minister of State for Finance, dated December 7, 2021, it was stated that total undisclosed credits of INR 20,353 Cr were detected with respect to 930 India linked entities in Panama and Paradise Paper leaks.

The Minister further stated that the income-tax Department takes appropriate action including search & seizure, survey, assessment, reassessment, levy of penalty etc., in case of persons, who are found to be involved in violations of various acts administered by the income-tax department. He also stated that in 52 cases of Panama and Paradise paper leaks, criminal prosecution complaints have been filed under the Black Money and Imposition of Tax Act, 2015 and in 130 cases, proceedings have been initiated under the said Act. Also, INR 153.88 Cr has been collected as taxes so far in Panama and Paradise Paper leaks.

The Minister also acknowledged that some Indian names have been released in the media which are allegedly linked to the Pandora Papers Leak and clarified that the Government has taken cognizance of it.

***Katalyst Comments:***

*Earlier in a press release dated October 4, 2021, the CBDT had acknowledged the Pandora Paper leaks by the International Consortium of International Journalists (ICIJ) and assured relevant investigations in such cases and set-up a Multi-Agency Group (MAG) headed by the Chairman, CBDT.*

[8] Release ID: 1778932 dated December 7, 2021

## B. Corporate Law Highlights

### 1. NCLT Kerala: RP, not an Adjudicating Authority, cannot determine quantum of claims[9]

CIRP was initiated by the Financial Creditor (the Applicant), the Federal Bank limited, against a Corporate Debtor. The Applicant filed claims against the Corporate Debtor, amounting to INR 3.7 Cr. In the Claim Verification Order issued by the RP, the claim of the Financial Creditor was rejected, claiming that the Applicant was not a Financial Creditor and that the Term Loan Agreement dated March 22, 2017 executed between the Applicant and the Corporate Debtor was novated by the Settlement Deed dated September 4, 2019, by which the amount was fully and finally settled.

Pursuant to the appeal filed by the Applicant, the NCLT ruled that RP was not an adjudicating authority and was not required to enquire into the factual scenario between parties and determine their rights and liabilities. The Tribunal elucidated that the RP's task was to limit itself to confirming that the claims received by him were true and correct and that verification was a process of establishing truth, accuracy or validity of the claim, which was not meant for making a decision on the quantum of claim. The Tribunal referred to Section 18 and Section 25 of the Insolvency and Bankruptcy Code, 2016, and highlighted that neither Section 18 nor Section 25 expressly cast a duty upon the IRP/RP to verify and admit or reject claims, and Regulation 13 of the Insolvency Resolution Process for Corporate Persons Regulations providing for the verification of claims. However, the RP failed to clear the contingency that existed in the amount and arrive at the best estimate of the amount of the claim based on the information available with him. Instead, the IRP outrightly rejected the claim of the Applicant without verifying the claim.

Accordingly, the NCLT held that the CIRP has disregarded the provisions of the IBC and the formation of the Committee of Creditors ('COC') was a nullity; the IRP would need to reconstitute the COC with the applicant financial creditor, and take further steps in relation to the CRP.

[9] [LSI-1001-NCLT-2021(KOC)] dated November 18, 2021

## 2. Delhi HC ruled in favour of the NCLT approval to sell Corporate-Debtor as 'going concern', foreclosed ED's property-attachment powers under PMLA[10]

M/s PSL Limited, the Corporate Debtor, was admitted to CIRP and the initially appointed Insolvency Professional was approved to be appointed as the liquidator by the Committee of Creditors (Petitioner). Post such appointment, the Liquidator issued a sale notice and subsequently received the summons from the Enforcement Directorate (ED/ Respondent).
The principal question which fell for determination in the instant writ petition was whether the authorities under the Prevention of Money Laundering Act (PMLA), 2002, would retain the jurisdiction to proceed against the properties of a corporate debtor once a liquidation measure has come to be approved in accordance with the provisions made in the Insolvency and Bankruptcy Code, 2016.

The Petitioner primarily contended that Section 32A clearly mandates that no action shall be taken against the properties of the Corporate Debtor, once a resolution plan comes to be approved or the corporate debtor undergoes liquidation. As per the Petitioner, the underlying objective of Section 32A has essentially been to ensure that a bona fide bidder in liquidation is protected from enforcement action.

In consideration of the contentions of the Petitioner, the Respondent, the Secured Creditors' and the Auction Bidders, the High Court held that:

- the principal consideration which appears to have weighed was the imperative need to ensure that neither the resolution nor the liquidation process once set into motion and fructifying and resulting in a particular mode of resolution coming to be duly accepted and approved, comes to be bogged down or clouded by unforeseen or unexpected claims or events. The IBC essentially envisages the process of resolution or liquidation to move forward unhindered;

- the issue of reconciliation between the IBC and the PMLA, in so far as the present case is concerned, needs to be answered solely on the anvil of Section 32A. Once the Legislature has chosen to step in and introduce a specific provision for cessation of liabilities and prosecution, it is that alone which must govern, resolve and determine the extent to which powers under the PMLA can be permitted in law to be exercised while a resolution or liquidation process is ongoing;

- introduction of Section 32A undoubtedly seek to allay such apprehensions and extend an assurance of the resolution applicant being entitled to take over the corporate debtor on a fresh slate. Section 32A assures the resolution applicant that it shall not be held liable for any offense that may have been committed by the corporate debtor prior to the initiation of the CIRP. It similarly extends that warranty in respect of the properties of the

[10] [LSI-1009-HC-2021(DEL)] dated December 15, 2021

corporate debtor once a resolution plan stands approved or in case of a sale of liquidation assets;

- from the date when the Adjudicating Authority came to approve the sale of the corporate debtor as a going concern, the cessation as contemplated under Section 32A did and would be deemed to have come into effect.

**Katalyst Comments:**

*The insertion of Section 32A, being a non-obstante provision has provided much-needed certainty and predictability, thereby safeguarding parties who may have acquired bona fide interest in the properties of the corporate debtor.*

### 3. IBBI clarifies that no NOC/ NDC required for voluntary liquidations[11]

Highlighting the time-bound period of 30 days for submission of claims under the IBBI (Voluntary Liquidation Process) Regulations, 2017, it was noted that the liquidators have been asking for No Objection Certification / No Dues Certificate ('NOC/NDC') from the Income Tax Department, thereby consuming substantial time and defeating the objective of time-bound completion of process under the IBC Code. IBBI observed that neither the Code nor the voluntary liquidation regulations envisage seeking such NOC/NDC. IBBI further provided that Section 178 of the Act provides "provisions of this section shall have effect notwithstanding anything to the contrary contained in any other law for the time being in force except the provisions of the Code.". Therefore, IBBI clarified that an Insolvency Professional handling voluntary liquidation process is not required to seek any NOC/NDC from the Income Tax Department as part of compliance in the said process.

***Katalyst Comments:***

*This is a welcome move particularly in such critical scenarios that may occur as a result of the ongoing pandemic. While negating the practice of seeking a NOC/ NDC from the Income Tax Department, the process of voluntary liquidation would be operationally efficient.*

[11] CIRCULAR No. IBBI/LIQ/45/2021 dated November 15, 2021

## C. Securities' Law Highlights

### 1. SEBI's informal guidance on approval of related party transactions pursuant to Regulation 23 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2008[12]

The Applicant, India Infradebt Limited, a public limited company is engaged in the business of Infrastructure Debt funding (NBFC SI ND). The Company finances infrastructure projects through secured and unsecured Non-Convertible Debentures (NCDs) by way of private placement. The Company was formed by four lending financial institutions viz., ICICI, Bank of Baroda, Citicorp Finance India Limited and LIC of India. The Company sought 'informal guidance' from the SEBI, on the application of Regulation 23 of the SEBI (LODR) (fifth amendment) Regulations, 2021 dated September 7, 2021, which requires high value debt listed companies to obtain approval from the shareholders on all material related party transactions which also, provides no related party should vote, whether or not such related party was a party to the transaction being approved or not.

However, proviso to Section 188(1) of the Companies Act, 2013 provides an exemption to a company in which 90% or more members, in number, are relatives of promoters or are related parties, enabling related parties to vote on related party transactions.

In this respect, the SEBI provided that in terms of the definition of related party under the provisions of Companies Act, the members of the Applicant are a "related party". Further, in terms of regulation 23(4), 23(7), 23(6) and 23(8), the existing and prospective material related party transactions would require shareholders' approval, with no related party to vote. However, SEBI stated that the Applicant's case fell in Explanation 3 to Regulation 15(1A) of LODR Regulation, which provides that the Companies not being able to comply with the afore-mentioned requirements should issue reasons for non-compliance or partial compliance in the quarterly compliance report on corporate governance filed with the Stock Exchange.

### 2. SEBI issued FAQs on SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021[13]

SEBI has issued FAQs on SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021. Some of the key takeaways are as follows:

- Contractual employees are also eligible to receive benefits under the Share Based Employee Benefit Scheme, provided they are designated as employees by their employers and are exclusively working with such company or its group company, including subsidiary or its associate company or its holding company;
- The provisions of the ESOP Regulations shall be applicable to Restrictive Stock Units. Phantom stock options would not be covered under these Regulations;

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[12] SEBI/HO/DDHS/P/OW/2021/37583/1 dated December 16, 2021
[13] Issued on November 16, 2021

- To meet regulatory requirements, an existing Scheme(s) may be amended to include the new class of employees without seeking shareholders' approval;
- Shares held by Trust shall be taken into account for the determination of percentage of voting rights under the SEBI Takeover Regulations.

### D. RBI/ Foreign Exchange Laws

### 1. RBI issues Prompt Corrective Action (PCA) Framework for NBFCs to further strengthen supervisory tools[14]

RBI issued Prompt Corrective Action (PCA) Framework for NBFCs, w.e.f. October 1, 2022 based on the financial position of NBFCs on or after March 31, 2022. The Bank observed that the NBFCs are growing in size and have substantial inter-connectedness with other segments of the financial system, and therefore, a PCA Framework for NBFCs has been put in place to further strengthen the supervisory tools applicable to NBFCs.

PCA Framework to be applicable on following types of NBFCs:

- All Deposit taking NBFCs (excluding Government Companies)
- All Non-Deposit taking NBFCs in Middle, Upper and Top Layers (including Investment and Credit Companies, Core Investment Companies Infrastructure Debt Funds, Micro Finance Institutions and Factors, but excluding NBFCs not accepting/ not intending to accept public funds, Government Companies, Primary Dealers and Housing Finance Companies)

The Bank provided that a NBFC would generally be placed under PCA Framework based on the audited Annual Financial Results and/or the Supervisory Assessment made by the Bank.

For invocation of PCA, the Bank prescribed the three risk thresholds under multiple parameters for different types of NBFCs and also tabulates the mandatory and discretionary actions under the framework for each of the three thresholds.

Further the Bank provided that once an NBFC is placed under the PCA, taking the NBFC out of PCA Framework and/or withdrawal of restrictions imposed under the PCA Framework will be considered:

- if no breaches in risk thresholds in any of the parameters are observed as per four continuous quarterly financial statements, one of which should be Annual Audited Financial Statement (subject to assessment by RBI); and

[14] RBI/2021-22/139 DoS.CO.PPG.SEC.7/11.01.005/2021-22

- based on Supervisory comfort of the RBI, including an assessment on sustainability of profitability of the NBFC.

The Bank has prescribed the corrective action basis the threshold breached as:

- caused by triggering the first threshold, will face restrictions on dividend distribution and promoters will be asked to infuse capital and reduce leverage;
- upon hitting risk threshold 2, the NBFC will be prohibited from opening branches;
- on risk threshold 3, capital expenditure will be stopped other than for a technological upgrade.

***Katalyst Comments:***

*The aforementioned regulations by the RBI follow the scale-based regulations concept and revision in non-performing asset (NPA) norms brought in by the regulator for the sector. Also, with the increasing size and operations of the NBFCs, and therefore, increasing regulations, brings NBFCs almost on par with banks in terms of supervisory reach.*

### 2. RBI revised benchmark rate for Foreign Currency ECBs and Trade Credits given discontinuance of LIBOR[15]

In view of the discontinuance of LIBOR as a benchmark rate, the RBI revised the all-in-cost benchmark in Master Direction – External Commercial Borrowings (ECBs), Trade Credits (TCs) and Structured Obligations (as amended from time to time). As a change, any widely accepted interbank rate or alternative reference rate (ARR) applicable to the currency of borrowing could be used as a benchmark, post discontinuation. As per the Circular, to take into account differences in credit risk and term premia between LIBOR and the ARRs, for new foreign currency ECBs and TCs, the all-in-cost ceiling has been revised from 450 bps to 500 bps and from 250 bps to 300 bps, respectively, over the ARRs. To enable transition of existing ECBs and TCs linked to LIBOR, it has been proposed to revise the all-in-cost ceiling from 450 bps to 550 bps and from 250 bps to 350 bps respectively, over the ARR.

## E. Goods and Service Tax Highlights

### 1. When the first summons is issued, the assessee should be given breathing time before issuance of further summons[16]

The Punjab and Haryana High Court has held that, in case when a first summons is issued and assessee has asked for time limit to submit documents, no further summons should be issued. The assessee should be given breathing time to submit the documents.

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[15] RBI/2021-22/135 A.P. (DIR Series) Circular No. 19 dated December 8, 2021

[16] Subway Systems India Pvt Ltd. vs. UOI [TS-639-HC(P&H)-2021-GST]

***Katalyst Comments:***

*The practice of issuing summons to top management and recovering money before issuance of show-cause notice has been observed under the GST regime. The decision of the Punjab and Haryana High court will support the assessee in case where multiple summons are issued without giving sufficient time to submit documents and reply.*

### 2. No separate GST registration required for dispatch of imported goods directly from Customs port in a State having no other fixed place of business[17]

Applicant intended to know whether Tax Invoice from registered place of business in Bengaluru office could be raised for imports received at Chennai Sea Port and directly sold to a customer either in Andhra Pradesh, Tamil Nadu, etc., or a separate registration is to be obtained at the place of Importation, i.e., Tamil Nadu and whether ITC is available in such instances or not.

In this regard, the Authority got Advance Ruling ('AAR'), Karnataka has held that since the applicant does not have any place of business in Tamil Nadu and does not maintain any office / fixed establishment in Tamil Nadu or any other state in India other than Karnataka, the applicant is not required to take any separate registration at the place of importation i.e. Tamil Nadu and ITC of said import is available if the goods are used for the purpose of business as per the provisions of section 20 of the IGST Act read with section 16 of the CGST Act.

***Katalyst Comments:***

*A welcome ruling by the Karnataka AAR. The taxpayer, depending upon the facts of the case may follow the 'Bill-to Ship-to model' wherein the goods can be 'Billed to Karnataka' and 'Shipped to Tamil Nadu' directly.*

### 3. Contribution made by society members for maintenance charges construes 'consideration' for supply of service and liable to GST[18]

The Maharashtra AAR holds that contribution by members towards maintenance charges is liable to GST due to the fact that the principle of mutuality is not applicable in lieu of amendment in definition of 'supply' u/s 7 of the CGST Act and the society and its members are distinct persons. Also, definition of business also includes provision of service by society to its members. The AAR also clarified that if contribution per member per month exceeds Rs. 7500/-, full amount is liable to GST. Further, regarding contribution towards sinking fund, building and repair fund and electricity fund, it is held that these contributions are towards

[17] In the matter of Pine Subsidiary Industry [TS-614-AAR(KAR)-2021-GST]
[18] In the matter of Mahindra Splendour CHS Ltd. [TS-657-AAR(MAH)-2021-GST]

the future supply of service and hence, GST is also payable on collection of such fund. In addition to the above, w.r.t. heavy repairs and maintenance expenses of society premises which are not capitalized, the AAR clarified that ITC of the same is available as the restriction-imposed u/s 17(5) (d) read with the explanation to such section is to the extent of capitalization.

***Katalyst Comments:***

*The definition of 'supply' has been amended by the Finance Act, 2021 but it is yet to be notified. Further, the ruling by the AAR is mainly based on the circular no. 109/28/2019-GST dated July 22, 2019.*

### 4. GST applicable on recovery of notice pay, insurance premium of parents and canteen expenses by the employer from the employee[19]

The Madhya Pradesh AAR has held that when employer recovers notice-pay and relieves an employee without fulfilling the notice period or accepts a shorter notice period, it is classified as "tolerating an act of employee…." as provided under schedule II and the same is liable to GST as supply of service. Further, w.r.t. insurance premium of non-dependent parents recovered by the employer; the AAR has held that the employer does not act as an agent of insurance company for recovery of such insurance premium and the transaction of recovery of insurance premium of parents is for the purpose of business and liable to GST. Further, regarding canteen expense recovery, the AAR has held that services provided by the employee to the employer is exempt. The canteen expense recovery is towards services provided by employer to employee and hence, GST is applicable.

***Katalyst Comments:***

*The Madhya Pradesh AAR has given a different ruling from the ruling of Maharashtra AAR in the matter of recovery of insurance premium by the employer from the employee. The Maharashtra AAR, in the similar matter, in case of Tata Motors Limited and POSCO India Pune Processing Centre (P) Ltd has held that no GST is payable on insurance premium recovery by the employer as employer is not into the business of insurance and hence, said activity is not covered within the purview of supply.*

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[19] In the matter of Bharat Oman Refineries Ltd [TS-652-AAR(MP)-2021-GST]

## 5. GST payable on sale of developed land for smart city development

The applicant is a public company, equally managed by Madhya Pradesh Urban Development Company Limited and Bhopal Management Corporation with an objective of planning and implementing "Smart City Project" in Bhopal. Under the Smart City Project, the applicant sales the developed plot of land post carrying out the development activities or providing amenities such as electricity line, drainage line, water line, land levelling, street lights etc. and construction activities are carried out by the buyers own their account and cost. The ownership of the land will get transferred in the name of buyer after payment of full value of consideration and execution of conveyance deed and not at the time of allotment of land to the buyer. The Madhya Pradesh AAR with respect to GST applicability on sale of developed plot of land has held that GST on sale of land per se is exempt as per schedule III of the CGST Act. However, in the instant case, sale of land is post development activities and hence, GST is applicable on sale of plot of land.

***Katalyst Comments:***

*The AAR has not considered the argument that only plot of land is transferred to the buyer. The amenities provided by the company are not transferred to the buyer. Further, definition of 'land' as provided under the Land Acquisition Act, 1894 provides that the land includes benefit arising out of land and thing attached to the earth or permanently fastened to anything attached to the earth. However, the said definition is also not taken into the consideration by the AAR.*

**Our Offices:**

**Mumbai**
71/75 Mittal Tower,
7th Floor, C Wing,
Nariman Point,
Mumbai - 400021
Tel: +91 22 4917 1616

**Pune**
#406-408,
Global Square, Near Bund-Garden,
Yerwada, Pune- 411006
Tel: +91 20 4840 7700