Katalyst Kaleidoscope

February 2019: Tax and Regulatory Insights

A. Income-tax Highlights

1. Bombay HC - Transfer of shares of a company cannot be considered as transfer of undertaking

- The Bombay HC[1], rejecting revenue's appeal, held that transfer of shares of a subsidiary company is taxable as capital gains under section 45 of the Income Tax Act, 1961 ("ITA) and cannot be considered to be a Slump Sale transaction within the provisions of section 2(42C) of the ITA.

- As per the facts of the case, the shares of the subsidiary were transferred for cash consideration. The HC, relying upon the Supreme Court judgement of Vodafone International Holdings[2] and Bacha F. Guzdar[3], observed that the interest of a shareholder does not amount to more than a right to participate in the profits of the company. As such, in the context of the case, it was held that, transfer of shares of the subsidiary does not result in transfer of undertaking of the subsidiary.

  Katalyst Comments:
  Under the ITA, a Demerger is tax neutral if the conditions under section 2(19AA) are satisfied. One of key conditions prescribed therein is transfer of an undertaking (i.e. a business activity and not individual assets and liabilities). While this was a case only involving shares of the subsidiary, the situation should be different if there is a demerger of an undertaking plus related shares.

2. ITAT Mumbai - Non-commercial loan between group entities cannot be construed "deemed dividend" under section 2(22)(e) of the ITA

- The assessee firm and a sister company were directly held by a common set of individual promoters. During the AY 11-12, the assessee and the company had undertaken number of current account transactions for receipts and payments such that, at the end of the FY, the books of the accounts of the assessee showed a net payable (i.e. loan) towards the company. The revenue contended, the loan received by the firm should be chargeable to deemed dividend as per section 2(22)(e) of the ITA.

- The ITAT, basis the provisions of section 2(22)(e) of the ITA and relying upon the judgement of the Supreme Court[4] in the case of Madhur Housing, held that the provisions of deemed dividend cannot be levied in the hands of the receiving entity if the entity is not a registered shareholder of the company.

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[1] Pr. CIT – 16 v. UTV Software Communications Limited (Income tax appeal no. 1475 of 2016) (Bombay – HC)
[2] Vodafone International Holdings B.V. v. Union of India [2013] 341 ITR 1/204 Taxman 408/17 taxmann.com 202 (SC)
[3] Mrs. Bacha F. Guzdar v. CIT [1955] 27 ITR 1 (SC)
[4] CIT v. Madhur Housing & Development Co. [Civil Appeal No. 3961 of 2013, dated 5-10-2017] (SC)

- Further, the ITAT also held that, current accommodation entries (i.e. receipts and payments in the normal course of business from a group entity), cannot be regarded as loans and advances for the purpose of section 2(22)(e) of the ITA.

- Basis the above, the ITAT[5] held in favour of the assessee, that the net payable to the group company cannot be treated as deemed dividend in the hands of the firm.

Katalyst Comments:
It is to be noted that, pursuant to amendment to section 115-O carried under the Finance Act 2018, deemed dividend received pursuant to section 2(22)(e) of the ITA shall be taxable in the hands of the payer-company at the rate of 30%. Consequently, the relevance of the above judgement would need to be evaluated in the present scenario, wherein, the tax would not be levied in the hands of the recipient entity but in the hands of the payer-company itself.

3. Supreme Court - Waiver of unsecured loan not claimed as deduction or allowance by the assessee during the previous years is a capital receipt and not liable to tax under section 41(1) of the ITA

- In view of the mounting losses and doubtfulness of repayment of unsecured loan, the assessee along with its creditor, being the parent company, agreed to convert the unsecured loan partly into equity and waive the balance as not recoverable. The AO held that, as the loans were received during ordinary course of asseesee's business with its parent company, the loan is a trading liability and waiver of trading liability is taxable under section 41(1) of the ITA.

- Aggrieved by the order of the CIT(A) and HC, who ruled in favour of the assessee, the Revenue filed an appeal with the Supreme Court. The Supreme Court, relying on its judgement in the case of Mahindra and Mahindra[6], dismissed the appeal of the revenue and ruled in favour of the assessee.

- It is pertinent to note that, as per the judgment of the Supreme Court in Mahindra and Mahindra, for the assessee to be liable to tax as per section 41(1) of the ITA, the assessee should have claimed any allowance or deduction in any previous year in respect of the trading liability; subsequently, the creditor remits or waives any such liability. The objective is to make ensure that the assessee does not get away with a double benefit once by way of deduction of interest and another by not being taxed on the benefit received by him in the later year with reference to deduction allowed earlier in case of remission of such liability.

Katalyst Comments:
The above judgement of the Supreme Court would be critical for companies undergoing the IBC (as also ARC) resolution process in relation to there being no tax on loan waivers whether from banks or financial institutions or otherwise and whether

[5] Golani Brothers v. DCIT (ITA No. 2615/M/2017) (ITAT – Mumbai)
[6] Mahindra And Mahindra Ltd. v. Commissioner [2018] 93 taxmann.com 32 (SC)

the loan was taken for capital expenditure, working capital or for funding losses. One hopes that the CBDT will issue a circular to this effect.

4. **Sanctioning scheme of amalgamation not a bar for tax proceedings in regular course; amalgamation scheme not held up**

- As per the facts of the Scheme of Amalgamation[7], the Transferor Company had brought forward tax losses which could be carried forward and utilized to set off against the income of the Transferee Company. Herein, the income-tax department raised an objection that the scheme has been made to avoid taxes in the hands of the Transferee Company.

- The NCLT held that sanctioning of the scheme of amalgamation shall not hinder the income-tax department to proceed against the transferee company or any other entity for carrying out proceedings under the ITA, for recovery of pending income tax dues, including imposition of penalties etc.

5. **Conversion of Compulsorily Convertible Preference Shares ("CCPS") into equity shares could not be considered as transfer and be chargeable to capital gains tax – ITAT Mumbai**

- As per the terms of the CCPS held by the assessee, each CCPS was convertible into one fully paid up equity share. On conversion into equity, the AO and CIT(A) assessed the conversion as Transfer as "exchange" under section 2(47) of the ITA. Consequently, capital gains tax was levied basis the FMV of the equity shares and cost of acquisition of CCPS.

- The ITAT, relying upon the CBDT Circular[8], held that conversion of one type of share into another cannot be deemed to be "exchange" of any share as the pre-converted security (CCPS) has ceased to exist. Exchange refers to a transaction involving barter, swap, etc.; consequently, the ITAT held that conversion of CCPS into equity shares cannot be treated as Transfer within the meaning of section 2(47) of the ITA.

- Further, it is pertinent to note the ITAT further held that, chargeability of capital gains tax on conversion of CCPS into equity would lead to double taxation in-as much as, having taxed the capital gains on conversion, upon sale of shares, the capital gains tax would be computed by deeming the issue price of CCPS as cost of acquisition pursuant to section 55(2)(b)(v) of the ITA and not the consideration adopted while levying capital gains on conversion.

Katalyst Comments:
As per the Finance Act, 2017, pursuant to section 47(xb) of the ITA, with effect from April 1, 2018, conversion of preference shares into equity shares is not regarded as a

[7] Company Petition No. (CAA) – 35 (PB) of 2018 in Aadhunik Realtors Private Limited dated 14th January, 2019 (NCLT Bench – Delhi)
[8] CBDT Circular F. No. 12/1/84-IT(AI) dated 12-5-1964

Transfer under the ITA and is therefore not chargeable to capital gains tax. Further, on transfer of equity shares post conversion, the cost of acquisition shall be the issue price of CCPS and the period of holding would be computed from the day of holding of CCPS. However, if the analogy referred in the above case can also be drawn upon for conversion of warrants is yet to be seen.

6. **Post retirement and relinquishment of rights and interest by the retiring partners, the properties of the firm explicitly belong to the firm and not to the retiring partners, thereafter, sale of any property would be chargeable to capital gains in the hands of the firm – Karnataka HC**

- On admission, Partner 1 and Partner 2 had contributed land along with a building constructed on it as capital contribution to the assessee firm. Later, the partners retired from the assessee firm and executed a release deed in favour of the continuing partners of the firm. Subsequently, approx. 20 years later, the assessee firm sold both the properties. However, owing to pending disputes between the retired partners and the assessee for both the properties, the sale deed for both the properties mentioned payment of certain share of sale value to the retiring partners to relinquish their rights and settle the disputes.

- The ITAT observed that, the nature or facts of the disputes have not been submitted with the it; consequently held that, on retirement of the erstwhile partners and execution of the release deed, they were no more the owners of the properties in question. Therefore, merely because they have mentioned in the sale deeds about relinquishing their rights does not pre-suppose that any right existed with them.

- The ITAT held that, the partners can only relinquish what they possess. In the present case, the erstwhile partners had no rights and the assessee was the rightful owner of both the properties; therefore, on sale of both the properties, regardless of assessee receiving the full consideration or not, entire capital gains shall be chargeable in the hands of the assessee firm.

7. **Relief for Startups – definition of Startup + Angel Tax**

- The Government has amended[9] the definition of "Startup" for the purpose of Income Tax Act, 1961. As per the amendments, a Startup means:

  - Turnover of the entity does not exceed INR 100 crores for any FY; (previously INR 25 crores); and
  - To be considered a Startup for a period of 10 years from incorporation (previously 7 years).

- Further, the notification has also provided exemption to Startups from Angel tax pursuant to section 56(2(viib) of the ITA on receiving aggregate investments (paid up share capital and share premium after the issue) upto INR 25 crores (previously INR

[9] Gazette Notification No. G.S.R. 127 (E) dated February 19, 2019

10 crores); this does not include shares issued to a non resident, a venture capital fund or a venture capital company. Also, amount received for shares to be issued to a listed company with certain specified thresholds is also not be so included.

Katalyst Comments:

- *While this is a welcome relief, the number of conditionalities for this notification are significant and the basic issue still remains that Section 56(2)(viib) is an outlier provision which is intended to possibly address unaccounted money being infused as share premium.*

- *Under the ITA, there are provisions such as section 56 and provisions to deal with sham transactions, as well as GAAR, but to introduce a provision like this and then create a whole set of carve out with so many conditions does not seem to be the appropriate way to address this. One hopes that the Government will recognize this fundamental issue and delete Section 56(2)(viib).*

8. CBDT forms two committees to examine and provide suggestions on International Good Practices and Litigation Management

- The CBDT has formed a 4-member committee, arising out of the Judicial Conference held on January 4, 2019, to examine as to how the International Good Practices on Tax Disputes and the diagnostic tool could be used for Tax Litigation Management. This committee is also to provide its report within one month of its formation.

- The CBDT has formed another 5-member committee to examine the issues and suggestions on Litigation Management arising out of the above Judicial Conference; the committee is to submit its report within one month of its formation. The committee's terms of reference include the following:

  - To examine the cases where ITAT has passed perverse or irregular orders or where the submissions of defendant's representative ("DR") have not been recorded by the ITAT to be appropriately taken up with President, ITAT/ Ministry of Law;
  - To examine the feasibility of creation of separate bench of ITAT for International Tax at places where the pendency of such cases is high / above a threshold limit;

Katalyst Comments:

- *The committee on international good practices on Tax disputes is a crucial committee in light of the huge litigation in India which seems to have no end point. It is hoped that the committee will consider matters from a completely different benchmark, including suggestions on preventing litigation, as opposed to only addressing issues on resolving litigation.*
- *The purpose of the 2nd committee is not clear. As mentioned above, one of the terms of reference of the above committee is to examine the cases where the ITAT has passed "perverse" or irregular orders. The aspect regarding "perverse" or irregular orders is not clear herein. It appears that the tax administration seems concerned about the fact that there are more favourable than adverse orders being passed by the*

Tribunal. Further, it could be that such orders, whether passed against the revenue or not, are very subjective in nature but it is unclear why these are considered "perverse" and what this committee is to achieve.

B. Foreign Exchange Regulations

1. RBI permits tapping of External Commercial Borrowings for companies undergoing the insolvency resolution process under the Insolvency and Bankruptcy Code, 2016

- As per the revised ECB regulations[10] and framework[11], an Indian Entity is permitted without the specific approval of the RBI to utilize ECB proceeds towards repayment of rupee loans provided that, the ECB has been raised either through the foreign equity parent or from a group company with common overseas parent.

- Further, in all other cases, an eligible borrower will have to take approval of the RBI towards utilizing ECB proceeds for repayment of rupee loans.

- In furtherance to the above, the RBI vide its Statement[12], has proposed to allow the resolution applicants under the approval route to utilize the ECB proceeds for repayment of rupee term loans of companies undergoing the insolvency process under the IBC Code. Guidelines in this regard shall be issued by the RBI at the end of February 2019.

Katalyst Comments:
Although, under the existing ECB framework, an eligible borrower can utilize the ECB proceeds for repayment of rupee loans subject to approval of the RBI, the statement issued by the RBI seems to suggest that RBI intends to simplify the approval route for resolution applicants for companies undergoing IBC proceedings by providing standard guidelines towards receiving RBI's approval.

2. Ease in investment by Foreign Portfolio Investors

The RBI vide its notification[13] has withdrawn the restriction for FPIs towards maintaining exposure of not more than 20% of its corporate bond portfolio to a single corporate (including exposure to entities related to the corporate).

Katalyst Comments:
As mentioned in the May 2018 edition of Katalyst Kaleidoscope, under the erstwhile framework notified on April 27, 2018, the FPIs were to comply with above requirement by March 31, 2019. Relaxation of this restriction would encourage a wider spectrum of

[10] FEMA (Borrowing and Lending) Regulations, 2018 [FEMA 3(R)/2018-RB]
[11] External Commercial Borrowings (ECB) Framework Policy – New ECB Framework dated January 16, 2019
[12] Statement of Developmental and Regulatory Policies issued by the RBI on February 7, 2019
[13] RBI/2018-19/123 dated February 15, 2019

investors to access the Indian corporate debt market. (Our KK for May 2018 can be accessed here)

3. Merger / Harmonisation of various categories of NBFCs

In light of the various categories of the NBFC pertaining to specific sector / asset classes, the RBI vide its Statement[14] has decided to harmonise the NBFCs engaged in credit intermediation viz. Asset Finance Companies (AFC), Loan Companies and Investment Companies, into a single category. As per the Statement, the proposed merger would cover 99% of the NBFCs in India, and, such merger would significantly reduce the complexities arising from multiple categories of NBFCs and also provide such NBFCs greater flexibility in their operations. The Guidelines are to be issued by the end of February 2019.

C. Corporate Law Highlights

1. Outbound demerger of Investment Undertakings under a Scheme of Arrangement – no adverse observations of SEBI

- As per the Scheme of Arrangement under section 230-232 read with 234 of the Companies Act, 2013 ("Act") involving Sun Pharmaceutical Industries Limited, ("the Transferor Company"), it has been envisaged that as part of internal organization, the Transferor Company shall:

  - Transfer the identified overseas direct investments to a direct wholly owned subsidiary based in Netherlands; and
  - Transfer its overseas direct investments in a US company to a indirect wholly owned subsidiary based in United States.

  As the Scheme of Arrangement is between a holding company and its wholly owned subsidiary company, no consideration is contemplated therein.

- The Appointed Date is defined to mean 1st April, 2017 or the date as approved by the NCLT and any government and regulatory authorities of United States, Netherlands and India.

Katalyst Comments:

- *The Scheme in effect deals with transfer of certain outbound investments which could have been transferred prospectively under a board and general / special resolution. However, the Scheme is contemplated to retrospectively transfer the investments with effect from 1st April, 2017. It is to be noted that, compliance with the RBI Cross Border Merger Regulations is imminent as captured in our KK April edition which can be accessed here.*

[14] Statement of Developmental and Regulatory Policies issued by the RBI on February 7, 2019

- *It is pertinent to note that the Scheme of Arrangement envisages exemption from capital gains on transfer of investments under section 47(iii) of the ITA as no consideration is contemplated under the scheme. (Note - Section 47(iii) provides for exemption from capital gains on transfer of any capital asset as "gift").*

2. On piercing the corporate veil for evaluating the fairness and intention behind the Scheme, the NCLT found the scheme to be unfair and consisting of malefic contents and proceeded to reject the Scheme

- The composite scheme of arrangement[15] involving UFO Moviez India Limited ("UFO Moviez"), a company listed on the BSE and NSE, and its group entities, contemplated a complex series of demerger, merger, sale of shares, capital reduction, and slump sale, wherein the following was envisaged:

  - Slump sale of IP Business Undertaking at fair value to the WOS of UFO Moviez; and
  - Providing exit to UFO Moviez's investors ("Investors") by utilsing the company's own resources.

- As per the report of the Regional Director submitted with the NCLT Mumbai Bench, the RD had several observations on the Scheme. The NCLT on hearing the representations of the RD sought to pierce the corporate veil of petitioner companies and held the composite scheme of arrangement to be "highly camouflaged, evasive, not logical, unfair, flouting of various laws, influencing the stock market, against public interest and, illegal".

- A few reasons given by the NCLT for rejection of the Scheme are as follows:

  - Alleged circumvention of buyback provisions under the Companies Act, 2013;

  - Alleged unjustified transfer of IP rights between shell group companies;

  Katalyst Comments:
  As per the section 230-232 of the Act, a company may enter into any arrangement with its members subject to approval of the NCLT. It is not clear as to why the arrangement contemplated under the Scheme was dismissed by the NCLT since the interest of the minority shareholders or the interest of the shareholders at large does not seem to be compromised.

3. Capital reduction of majority shareholders without paying/returning any consideration to the shareholders is not permitted under section 66 of the Act

- On February 4, 2019, the NCLT Mumbai Bench held[16] that the reduction of share capital of majority shareholders of a company without paying any consideration to them

[15] C.P. (CAA) No. 1920 of 2018 in UFO Moviez India Limited dated 12th February, 2019 (NCLT Bench – Mumbai)
[16] Ansa Decoglass Private Limited (CP No. 79 of 2018 dated February 4, 2019) (NCLT Mumbai)

and crediting the same amount to the capital reserves is not envisaged under section 66 of the Act.

- The NCLT also observed the Scheme to be "strange" for non-payment of any consideration in light of the strong fundamentals of the company's balance sheet.

Katalyst Comments:
In a separate decision[17], the NCLT Mumbai Bench on January 4, 2019, has approved capital reduction of only non-promoter shareholders on repayment of capital to them. It seems that the NCLT view is that reduction of share capital without pay-out is not permitted, although no explicit provision restricting the same is mentioned under section 66 of the Act.

4. MCA revisits Significant Beneficial Ownership rules – Lesser ambiguities & more onus on the reporting company

- The MCA vide a recent notification[18] amended the Companies (Significant Beneficial Owners) Rules, 2018. While the condition of disclosure of all individuals directly and indirectly holding atleast 10% of the voting rights / shares of the company remains sacrosanct, the amendments have sought to bring in more clarity, removed ambiguities and, tilted the onus of responsibility towards the reporting company along with its shareholders.

- The amended regulations have also increased the already high number of compliances under the Act.

- The key amendments are as follows:

#	Particulars	Reporting under the present framework	Reporting under the new framework	Takeaway
1	**Definition of Significant Beneficial Owner ("SBO")**	An individual holding ultimate beneficial interest of not less than 10%.	An individual, acting alone or together, holding either 10% shares / voting rights / distributable dividend or possesses the right to exercise significant influence.	Wider definition and increased subjectivity for identification of SBOs.
2	**Determining the individuals who are SBO of the reporting company**			
2A	If the member is a **Company**	Individuals acting together, holding not less than 10% of the share capital or who	Individuals directly + indirectly has a right to receive more than 50% of shares / voting rights /	Providing a higher threshold limit of 50% vis-à-vis 10%.

[17] ARI Consolidated Investments Private Limited (CP No. 1501/66 of 2018 dated January 7, 2019) (NCLT Mumbai)
[18] Companies (Significant Beneficial Owners) Amendment Rules, 2019 dated February 8, 2019

#	Particulars	Reporting under the present framework	Reporting under the new framework	Takeaway
		exercises significant influence or control	distributable dividend in the company or its ultimate holding company.	
2B	If the member is a **firm/LLP**	Individuals acting together, holding not less than 10% of the profits / capital.	Individual partners OR if the partner is a body corporate, provisions of para 2A above to be followed.	Providing a more methodical manner for determination of SBOs which is also subjective in nature
2C	If the member is a **Trust**	Settlor, trustee and beneficiaries.	- Trustee in case of a discretionary / charitable trust - Beneficiary in case of a specific trust - Settlor in case of a revocable trust	Seems that individuals with whom effective control of Trust lies needs to be reported herein.
2D	If the member is a **pooled investment vehicle** (other than SEBI / RBI registered)	An individual holding the position of the Senior Managing Official	Individual being the: - General partner; or - Investment manager; or - CEO, as the case may be.	Rationalizing the identification of SBOs
2E	If the member is a **HUF**	NA	Karta	Clarity regarding HUFs.
3	**Duty of reporting company to seek information from shareholders**	NA	Reporting Company to seek information in Form BEN -4 from members (not being individuals) holding more than 10% for the determination of SBO.	Responsibility also on the company to seek identity of SBOs.
4	**Non-applicability to the extent the share of the reporting company is held herein**	Mutual Funds, AIFs, REIT and InVITs regulated under the SEBI Act	- Certain SEBI and RBI regulated investment vehicles - The holding reporting company of the reporting company.	Increasing the extent of non-applicability to RBI regulated investment vehicles.

#	Particulars	Reporting under the present framework	Reporting under the new framework	Takeaway
			- Investor Education and Protection Fund	

- Every individual shareholder, being a SBO as on the date of commencement of the amended regulations i.e. 8th February, 2019, shall file a declaration in Form no. BEN-1 with the reporting company within 90 days from such commencement.

Katalyst Comments:

- *Although the amended SBO rules have sought to reduce ambiguities in identification of a SBO, the high subjectivity under these regulations are prone to increasing difficulties for identifications while increasing the responsibility of the companies to a certain extent.*

- *As next steps, every reporting company is to seek information from non-individual shareholders holding more than 10% stake in Form BEN-4 and such shareholders to evaluate their SBO status and disclose it to the reporting company in Form BEN–1 within 30 days of receipt of Form BEN-4.*

- *In addition to the above compliances under the Act, listed companies are also required the report the Significant Beneficial Ownership with the stock exchanges in the format prescribed by the SEBI from quart ended 31st March, 2019. Kindly refer the December 2018 edition of Katalyst Kaleidoscope for more details here.*

5. Filing of one time return for outstanding money or loan not considered as deposits

- The MCA vide a notification[19] has amended the Companies (Acceptance of Deposits) Rules to provide that, every company, other than a Government Company, is required to file a onetime return of all outstanding receipt money or loan, received by the company from April 1, 2014 to January 22, 2019, which have not been considered as deposits under the Companies Act, 2013.

- The reporting is to be carried out in Form DPT-3 and has to be filed within 90 days of this amendment being published in the Official Gazette.

[19] Notification for Companies (Acceptance of Deposits) Amendment Rules, 2019 dated January 22, 2019

D. Securities Law Highlights

1. Consultation paper for proposed amendments in SEBI REIT and SEBI INVIT Regulations towards increasing their reach and flexibility

- With a view to increase flexibility of SEBI (Real Estate Investment Trusts) Regulations, 2014 ("REIT Regulations") and SEBI (Infrastructure Investment Trusts) Regulations, 2014 ("INVIT Regulations") and increasing their access to the investors, the SEBI vide a Consultation Paper[20] has proposed certain amendments to the regulations. The public comments on these proposed amendments were to be sent by February 18, 2019.

- The key amendments proposed in the regulations are as follows:

#	Subject	Present regulatory framework	Proposed regulatory framework	Takeaway
1	Reduction in minimum investment limit for subscription during initial offer	- INVIT INR 10 lakhs - REIT More than INR 2 lakhs	- INVIT and REIT INR 15,000-INR 20,000 per lot	Encouraging participation of retail investors
2	Reduction in minimum limit of a lot for the purpose of trading units on a stock exchange	- INVIT INR 5 lakhs - REIT INR 1 lakh	- INVIT and REIT Trading lot shall be of 100 units each with no minimum restriction on value.	Encouraging participation of retail investors
3	Increase in leverage limit for INVITs	Approval of unit holders required for borrowing above 25% of the value of INVIT assets, with the maximum limit fixed at 49%.	Increasing the maximum limit to 70% of the value of INVIT assets for acquisition of new infrastructure assets, subject to approval of 75% of the unit holders who are not related and certain other conditions.	Increase in INVITs ability to acquire new assets to support its growth in core value propositions.
4	Unlisted INVITs	- Mandatory listing of privately placed INVITs - Minimum 25% public participation in the listed INVIT	A new regulatory framework is being proposed for unlisted INVITs, wherein: - Flexibility with INVIT to decide Leverage, minimum number of investors, and their investment.	Providing more flexibility to unlisted INVITs and their private investors.

[20] SEBI Consultation Paper dated January 25, 2019

#	Subject	Present regulatory framework	Proposed regulatory framework	Takeaway
		- Prescribed minimum number of investors	- Listing shall be not mandatory; - Existing listed INVITs also given an option to delist.	

2. Amendment to the Insider Trading Regulations – Members of the Promoter Group to also to be disclosed

- As per the recent amendments[21] in the SEBI (Prohibition of Insider Trading) Regulations, with effect from January 21, 2019, all initial and continual disclosures under Regulation 7 of PIT Regulations shall also have to be complied by every member of the Promoter Group along with the Promoters.

- Promoter Group shall have the meaning assigned to it under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018.

Katalyst Comments:
Pursuant to the above amendment, the members of the Promoter Group would have to comply with the initial and continual disclosures obligations under the SEBI PIT Regulations.

E. Insolvency and Bankruptcy Code Highlights

1. Insolvency proceedings can be invoked against the corporate guarantor before proceeding against the principal debtor – Supreme Court

- As per the facts of the case, the financial creditor had sanctioned the loan to the principal debtor on provision of guarantee by the corporate guarantor. On the default of repayment of loan by the principal debtor, the financial creditor invoked the corporate guarantee for repayment of loan by the corporate guarantor. On failure to repay the loan by the corporate guarantor, the financial creditor filed an application for initiating insolvency proceedings against the corporate guarantor. The NCLT, in favour of the creditor, accepted the application.

- In an appeal by the shareholder of the corporate guarantor at the NCLAT against the order of the NCLT, the NCLAT held that as per the IBC Code, a corporate guarantor becomes a corporate debtor as soon as the guarantee is invoked. Further, it also held that the IBC Code does not bar a creditor to initiate insolvency proceedings against

[21] SEBI (Prohibition of Insider Trading) Regulations, 2015 ('PIT Regulations') dated January 21, 2019

the corporate guarantor (on failure of the principal debtor to repay the loans) without exhausting his remedies against the principal debtor.

- Thereafter, on an appeal with the Supreme Court by the shareholders of the corporate guarantor, the SC not only affirmed the order of the NCLAT but also held that, pursuant to amendment[22] of the IBC Code, the IBC Code recognizes the validity of a corporate guarantor and principal debtor in a lending agreement; therefore, the argument that the proceedings cannot be initiated against the corporate guarantor without first initiating proceedings against the principal debtor is redundant.

Katalyst Comments:
Consequent to the above judgement, a corporate guarantor shall have to evaluate repayment of loan by its group companies and on their default, by itself, to mitigate any insolvency proceedings against it.

2. Provision of Performance Security by the Resolution Applicant - Amendment to the Insolvency Resolution Process

- As per a recent amendment to the Insolvency Process for Corporate Persons[23], every resolution plan provided by a resolution applicant shall include a performance security of such nature, value, duration and source, as would be necessary pursuant to the approval of the committee of creditors.

- On approval of the resolution plan by the NCLT / adjudicating authority, the resolution applicant shall provide the performance security in such time as would be specified in the resolution plan.

- The performance security shall be forfeited, if after approval of the plan, the resolution applicant fails to implement or contributes to the failure to the implementation of the resolution plan in accordance with the terms of the plan and its implementation schedule.

- Further, as per the present amendment, a resolution applicant shall also state in the resolution plan whether the applicant or its related party, either has failed to implement or has contributed to failure to implement of any other resolution plan approved by the NCLT / adjudicating authority.

Katalyst Comments:
- *The mandatory provision of providing a performance guarantee is intended to act as a deterrent to frivolous and capricious resolution applicants.*

[22] Insolvency and Bankruptcy Code (Second Amendment) Act, 2018
[23] The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Amendment) Regulations, 2019 dated January 24, 2019

3. Appointment of erstwhile personnel of the secretarial auditors as insolvency professionals on Voluntary Liquidation

The Insolvency and Bankruptcy Board of India has amended the IBBI (Voluntary Liquidation Process) Regulations, 2017[24] to provide for appointment of an individual as an insolvency professional, if he has not been a partner / employee of the secretarial auditors (previously company secretaries) of the corporate person, at any time in the last 3 years.

F. Stamp Duty Highlights

Stamp duty on amalgamation and reconstruction introduced in Tamil Nadu Finance Bill

- The Tamil Nadu government in its Finance Bill 2019 has proposed an amendment in the Tamil Nadu Stamp Act towards levying stamp duty on property transferred through a scheme of amalgamation and reconstruction, as follows:

  i) 2% of the market value of the immovable property; or
  ii) 0.6% of the market value of shares issued.
  Whichever is higher.

- Further, Registration Fees of such transactions is proposed to be fixed at a maximum of INR 30,000/-

Katalyst Comments:
The proposed amendment brings in much needed clarity on applicability of stamp duty and registration fees in Tamil Nadu on property transfer through a scheme of amalgamation / reconstruction. To understand the ambiguity removed herein, refer the page 7 of our December KK here.

G. Indirect Taxation

1. AAR: EPC contract liable to 18% GST

The Maharashtra AAR[25] has held that EPC contract for metro project involving erection, testing and commissioning including transport, loading, insurance etc. of transformers substations, HT & LT overhead line & cable through underground etc. are not in the nature of 'original works' and therefore, concessional rate of 6% prescribed for railways, metro & monorail is not applicable and GST @ 18% is payable.

[24] Notification No. IBBI/2019-20/GN/REG039, dated January 15, 2019
[25] In the matter of Yogiraj Powertech Private Limited [TS-877-AAR-2018-NT]

2. Relaxation to advance authorisation holders

The CBIC[26] has removed the pre-import condition to avail exemption from IGST and compensation cess and benefit of advance authorisation has been extended to deemed exports from prospective effect, subject to the authorisation holder complying prescribed conditions.

3. Analysis of GST Notifications effective from February 1, 2019

- W.e.f. February 1, 2019, the GST Amendment Laws (except some specified provisions)[27] and GST Rules[28] are applicable.

- 'Supply' clarified
  Definition of supply has been retrospectively amended and the activities listed in schedule II will be taxable only if there is an underlying supply, and the schedule is relevant only for classifying the supply between goods or services.

- Registration

  - Any person having multiple places of business in a single state, has been allowed to obtain multiple registrations (subject to conditions) in a state which was allowed earlier for separate business verticals only. The concept of business vertical has been removed.
  - A person having unit in SEZ is required to take separate registration for another unit even if it is located in same state outside SEZ.

- Export of service

  The supply of service outside India can be said to be exported even if the consideration is received in Indian rupees, wherever permitted by RBI.

- Input tax credit('ITC')

  - ITC of ceases shall not be the part of transition credit.
  - No reversal of common credits required for the transactions of high sea sale, merchant trade transactions, supply of warehoused goods before clearance for home consumption and sale of actionable claims etc.
  - The credit balance of SGST and UTGST can be utilised for the payment of IGST, only if credit balance of CGST is not available.
  - ITC in respect of (i) motor vehicles used for transportation of persons having seating capacity of more than thirteen persons (including driver), vessels and aircraft; (ii) services of general insurance, repair and maintenance in respect of

[26] Notification no. 1/2019-Customs dated January 10, 2019
[27] Notification no. 2/2019-Central Tax dated January 29, 2019 & Notification no. 1/2019-Integrated Tax dated January 29, 2019
[28] Notification no. 3/2019-Central Tax dated January 29, 2019

motor vehicles, vessels and aircraft on which credit is available; and (iii) goods or services which are obligatory for an employer to provide to its employees, under any law for the time being in force etc. are available.

- Other amendments

  - GST under reverse charge mechanism is applicable to specified class of persons[29] on receipt of supply of specified categories of goods or services from unregistered suppliers. Specified categories of goods or services and specified class of persons are yet to be notified.
  - The place of supply for services of transportation of goods, where the transportation of goods is to a place outside India and the location of the supplier and recipient of services are in India, will be the place of destination of such goods
  - Threshold limit to opt for the composition scheme has been extended from 1 crore to 1.5 crore
  - Consolidated debit/credit note can be issued without linking the same with individual invoices
  - Taxes, penalty, fine etc. can be recovered from the distinct person (having same PAN & different GSTIN), even if such distinct persons are present in different states
  - Goods temporarily imported into India for any treatment/process are not liable to GST.
  - The commissioner has been empowered to increase the time line for return of input and capital goods, sent for job-work, upto 1 year and 2 years, respectively

H. Unregulated deposit scheme ordinance

- The banning of Unregulated Deposit Scheme Bill, 2018, was introduced in the Lok Sabha on 18th July 2018 and was referred to the Standing Committee on finance, chaired by Dr. Veerappa Moily, on 10th August 2018 for examination and report thereon. In pursuance thereof, the Committee considered and adopted their report on 2nd January 2019.

- In pursuance thereto, the Ministry of Law and Justice has issued an Ordinance date 21st February 2019 titled the "Banning of Unregulated Deposit Scheme Ordinance, 2019" ('the Ordinance'). The salient features are as under:

  i) The key objective is to prevent Unregulated Deposit Schemes ('UDS') which term has been defined as a scheme or arrangement under which deposits are accepted or solicited by any deposit taker by way of business and which is not a Regulated Deposit Scheme ('RDS').

  ii) RDS means a deposit scheme launched under SEBI, RBI, MHB, PFRDA, EPF etc. regulations.

[29] Notification no. 1/2019-Central Tax (Rate) dated January 29, 2019

iii) The heart of the Ordinance is that UDSs are banned and penalties are substantial.

iv) While several exceptions are provided and seem to give the impression that everything else is covered, it is important to note that in order to fall within the clutches of the ordinance, it should first be a "Scheme" and therefore, an organised fund raising and it does not seem to apply to individual loans.

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