

Katalyst Kaleidoscope

February 2023: Tax and Regulatory Insights

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A. Income Tax highlights

1. Supreme Court: Lessor being real owner of asset in case of a finance lease, lessee to be given deduction for lease rent paid¹

The Supreme Court upheld the Gujarat High Court decision where the lessor was held as the 'real owner' of an asset in the case of a finance lease, and not the lessee. The lessor, being the holding company of the lessee, disclosed lease rent as business income, and claimed depreciation on such leased asset, being the owner of the asset. Since the lessor is claiming depreciation, deduction for lease rent paid shall be allowed to the lessee in respect of the same transaction.

Katalyst Comments

1. *This decision once again reiterates the principle that for tax purposes, once the lessor is held to be the owner of the asset and eligible to claim depreciation, then the lease rent paid by the lessee can be claimed as revenue expenditure for tax purpose.*
2. *Incidentally, from an accounting perspective, IndAS 116 on Leases requires a lessor to recognise all assets held under a finance lease in its balance sheet as a receivable as on the commencement date, and the lessee is required to recognise a 'right of use asset', representing its right to use the underlying leased asset, and a corresponding lease liability representing its obligation to make the lease payments; to that extent, as is now happening in many situations, the tax and accounting treatments will diverge.*

2. Delhi High Court: TRC is a sufficient condition for claiming relief under a DTAA²

The Delhi High Court has held that a tax residency certificate ('TRC') is statutorily the only evidence required to be eligible for availing the benefit under the DTAA. The Hon'ble High Court placed reliance on the Finance Ministry's clarificatory press release dated March 1, 2013, stating that TRC produced by a resident of a contracting state will be accepted as evidence of residency of that contracting state and the Income Tax Authorities in India will not go behind the TRC and question his residential status. The tax authorities of the contracting state would have granted the petitioner the TRC after a detailed analysis of the documents, and the Indian tax authorities cannot disregard the same, as doing so would be contrary to international law.

In the above context, an Assessing Officer cannot issue re-assessment notice to an assessee questioning the residential status, treaty eligibility and legal ownership in spite of a TRC issued by another country, and accordingly, the re-assessment proceedings were quashed.

¹ CIT v Narmada Chematur Petrochemicals Ltd. (SC) dated January 20, 2023

² Blackstone Capital Partners (Singapore) Vi Fdi Three Pte. Ltd v ACIT 146 taxmann.com 569 (Delhi) dated January 30, 2023

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Katalyst Comments

The judgement re-iterates the principle that TRC is conclusive evidence for granting treaty benefit. Though the judgement is relating to the pre GAAR / MLI era, it may be still be contemporaneously relevant.

3. Mumbai ITAT: Assessment order passed on amalgamating company illegal³

The income tax authorities were notified of a scheme of amalgamation approved by the NCLT and were requested to direct all future communication relating to the amalgamating company to the amalgamated company as the successor; yet, assessment orders were passed in the name of the amalgamating company.

The Hon'ble ITAT held that the assessment orders have been passed in the name of the amalgamating company, which was non-existent as on the date of the order, and hence, the orders were held as illegal and invalid. The Mumbai ITAT relied on the Supreme Court judgement in the case of Maruti Suzuki⁴, where the apex court held that assessment on a non-existent entity is a substantive illegality.

The NCLT considered the objections and sanctioned the scheme; of course, this does not preclude the tax authorities from examining the compliance of tax consequences during the course of assessment proceedings.

B. Corporate Law Highlights

1. MCA: Transition to Version 3 filing system

The Ministry of Corporate Affairs ('MCA') is in the process of updating their online form filing portal from their current Version 2 to Version 3. In the process, 56 forms have been modified and become web-based vide an array of amendment rules, seeking additional disclosures. These forms are in relation to incorporation and registration of companies, allotment of securities and share capital, appointment and remuneration of managerial personnel, debentures and company accounts.

Some of the key modifications made in certain forms are:

- Reasons for disqualification of a director shall be specified by a company while filing Form DIR-9 with the Registrar.

³ Hindustan Unilever (as legal successor of Glaxo Smithkline Consumer Healthcare Ltd v DCIT (Mumbai ITAT) dated February 8, 2023

⁴ PCIT v Maruti Suzuki India Limited 107 taxmann.com 375 (SC) dated July 25, 2019

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- Residential status of managerial person being appointed via Form MR-1 shall be stated.
- Along with Form SH-11 for buyback of securities, a declaration certifying that the buyback is as per the provisions of the Act signed by two directors of the company, one being the managing director, shall also be filed.

Katalyst comment:

Several forms have till now required approval of the RoC and this was a major bottleneck in corporate actions; with the introduction of web-based forms, there is a move to only 'acknowledgement' of the RoC. This is extremely helpful, but needs far more broad basing and the MCA portal needs serious streamlining, since the procedural act of uploading is itself becoming an issue.

2. Chennai NCLT: Demerger v Slump Sale⁵

An entity filed a composite scheme of arrangement which included transfer and vesting of a business undertaking by way of slump sale to a group entity. The income tax department raised objections to the same, construing the proposed slump sale as a demerger and contending that the scheme does not fulfil the conditions for a demerger as per the Act; the petitioner companies clarified that a slump sale as per section 2(42C) of the Act was proposed in the scheme and not a demerger. The NCLT accepted the petitioner companies' contention.

The same scheme also involved merger of a wholly owned subsidiary with its holding company. While the income tax department objected that there is no issuance of shares in consideration of the merger, which is a condition under section 2(1B) of the Act, the petitioner companies contended that the section prescribes issuance of shares to shareholders of the transferor company other than shares already held by the transferee company in the transferor company prior to the merger. In the given case, it was contended by the petitioner since the transferor company is a wholly owned subsidiary of the transferee company, there is no requirement to issue shares and the conditions have been satisfied. The NCLT approved the scheme, but mentioned that the tax department is not precluded from looking into tax issues in the regular course later.

3. Ahmedabad NCLT: Alteration of Authorised Share Capital on Merger⁶

The petitioner companies filed a draft scheme of arrangement involving a merger as well as a demerger. The scheme sought to amalgamate the authorised share capital of the entities being merged without payment of additional fees and duties. It also sought to enhance the authorised share capital of the resulting company in order to issue shares to the shareholders of the demerged company.

⁵ Samunnati Financial Intermediation & Services P. Ltd & ors. CP(CAA)/SS(CHE)/2022 dated December 23, 2022

⁶Jay Chemical Industries Pvt Ltd & ors, C.A.(CAA)/19(AHM)2022 dated January 3, 2023

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The Regional Director required the petitioner company to comply with the provisions of the Act in relation to the alteration of authorised share capital. The petitioner companies have undertaken to comply with the provisions of section 61 r.w. section 232 of the Act in relation to merger and pay differential fee to the applicable extent in respect of enhancement of authorised share capital in relation to the demerger. The said corporate actions can be undertaken as an integral part of the scheme.

C. SEBI / RBI / Stamp Duty Highlights

1. SEBI: Listing Obligations and Disclosure Requirements ('LODR') amendments notified

SEBI vide its notification dated January 17, 2023⁷, has notified certain amendments to LODR; the key amendments are as follows:

- Corporate governance norms will be applicable to SEBI-registered InvITs and ReITs from April 1, 2023.
- The definition of 'senior management' is now amended to include functional heads. Consequently, the regulations applicable to senior management, such as on appointment and remuneration, shall now be extended to functional heads.
- Along with appointment of a person on the Board of Directors or as a manager, now even a re-appointment requires approval of shareholders at the next general meeting or within 3 months of the re-appointment, whichever is earlier.
- The details of material subsidiaries, including the date and place of incorporation and the name and date of appointment of the statutory auditors, should be disclosed in the corporate governance report for the annual reports filed for the F.Y. 2022-23 onwards.

Vide a separate consultation paper released on February 8, 2023⁸, SEBI proposed corporate governance rules for related party transactions for high value debt listed entities, which are entities having listed non-convertible debt securities of INR 500 Crore and above.

2. SEBI: Manner of Achieving Minimum Public Shareholding⁹

In order to facilitate the listed entities to achieve the minimum public shareholding of 25%, existing methods have been reviewed and rationalised. Further, two methods additional to the existing methods have been introduced by SEBI; the two new methods are as follows:

1. Allotment of shares via employee stock option, subject to a maximum of 2% of paid-up equity share capital in the listed entity.
2. Shares held by the promoter or promoter group transferred to an exchange traded fund managed by a SEBI-registered mutual fund, subject to a maximum of 5% of paid-up equity share capital in listed entity.

⁷ Securities and Exchange Board of India (LODR) (Amendment) Regulations, 2023 dated January 17, 2023

⁸ Consultation paper on review of Corporate Governance norms for a High Value Debt Listed Entity dated February 8, 2023

⁹ SEBI Circular No. SEBI/HO/CFD/PoD2/P/CIR/2023/18 dated February 3, 2023

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3. SEBI: Amendment in Buyback of Securities Regulations¹⁰

SEBI has introduced new regulations with respect to buyback of securities. The key amendments are as follows:

1. **Maximum limit for buyback:** While calculating the maximum limit of buyback (including for calculation of the debt-equity ratio), being 25% of paid up capital and free reserves, the amounts considered shall be as per standalone or consolidated financial statements, whichever is lower.
2. **Phasing out of buy-back from the open market through stock exchanges:** Open market buy-backs through stock exchanges will be completely phased out from April 1, 2025. The gradual phase-out of the open market buy-backs through stock exchanges, shall be achieved by limiting the quantum of buy back permitted to less than: (a) 15% of the paid up capital and free reserves of the company till March 31, 2023; (b) 10% of the paid up capital and free reserves of the company till March 31, 2024; and (c) 5% of the paid up capital and free reserves of the company till March 31, 2025.
3. **Lender Consent:** As a condition to buy-back, a prior lender consent shall be obtained in case of a breach of any covenant with such lender and a disclosure of the consent shall form part of the letter of offer.
4. **Minimum Buy-back utilization for Buy-back from Open Market:** At least 75% of the amount earmarked for buy-back (as specified in the board or special resolution) as against 50% under the current Buy-back Regulations shall be utilized for buying back shares or securities. Further, SEBI has now prescribed that at least 40% of the amount earmarked for buy-back is utilized within initial half of the specified duration.
5. **Buyback Procedure:** An offer procedure has been detailed, which also gives guidelines for the buyback price and its range. Retail promoters have been given the option to bid at the buyback price, and promoters and their associates shall not be permitted to participate in buyback through book building. A detailed methodology for acceptance of bids has also been prescribed. A host of other procedural amendments have been made.

¹⁰ Securities And Exchange Board of India (Buy-Back of Securities) (Amendment) Regulations, 2023, dated February 7, 2023

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4. SEBI: Introduction of Issue Summary Document¹¹

In order to facilitate ease of consumption of data by stakeholders, an issue summary document ('ISD') has been introduced in a phased manner. It will make available the relevant information / data points relating to public issue of specified securities (IPOs, FPOs), further issues (preferential issues, qualified institutions placement, rights issues, issue of American Depository Receipts, Global Depository Receipts, and Foreign Currency Convertible Bonds), buybacks, open offers, and voluntary delisting of equity shares to the stock exchanges and depositories in a structured manner, both at pre-offer and post-offer stage. The ISDs will be disseminated through the websites of the stock exchanges and depositories.

The implementation of filing of an ISD will be in the following phases:

- i. Public issue of specified securities: Offer documents filed on or after March 1, 2023
- ii. Further issues: April 3, 2023
- iii. Open offer, buyback and voluntary delisting: May 2, 2023

5. SEBI: Master Circular on Takeover Regulations¹²

In order to enable the stakeholders to have access to the provisions of all circulars relating to the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ('Takeover Regulations'), SEBI has released a Master Circular. This is primarily a consolidation of all existing and applicable circulars and formats for disclosures relating to Takeover Regulations.

Katalyst comment:

The concept of Master Circular is extremely helpful, since it becomes much easier to interpret one consolidated circular.

6. SEBI: Consultation paper on strengthening corporate governance¹³

SEBI has issued a consultation paper seeking comments and suggestions by March 7, 2023 in relation to the above; the consultation paper deals with the following issues:

- Agreements binding listed entities,
- Special rights granted to certain shareholders,
- Sale, disposal or lease of assets of a listed entity outside the 'Scheme of Arrangement' framework, and
- 'Board Permanency' at listed entities.

¹¹ SEBI Circular No. SEBI/HO/CFD/PoD-1/P/CIR/2023/29 dated February 15, 2023

¹² SEBI Master Circular No. SEBI/HO/CFD/PoD-1/P/CIR/2023/31 for Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, dated February 16, 2023

¹³ SEBI Consultation Paper on Strengthening Corporate Governance at Listed Entities by Empowering Shareholders dated February 21, 2023

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The key features are as under:

- 1. Agreements binding listed entities:** The consultation paper proposes that, in relation to agreements between shareholders where the listed entity is not a party to the agreement, there must be an obligation on such parties to disclose it to the company, and for the company to disclose it to the Stock Exchanges. Additionally, it is proposed that there should also be disclosure of the details of the agreement entered into during the financial year in the annual report of the listed entity. Further, there is also a proposal that the board of directors should provide its “opinion along with detailed rationale” as to “whether such an agreement is in the economic interest of the listed entity”. There are also transitional provisions proposed for disclosure of existing agreements.
- 2. Special rights granted to certain shareholders:** The consultation paper has mentioned that every listed entity should ensure equitable treatment of all shareholders including minority and foreign shareholders, and that, if any shareholder is enjoying special rights and privileges, the same should be agreed upon by all other shareholders of the company. Accordingly, the consultation paper proposes that any special rights (existing/proposed) granted to a shareholder shall be subject to shareholders approval once in every 5 years from the grant of such special rights.
- 3. Sale, disposal or lease of assets of a listed entity outside the ‘Scheme of Arrangement’ framework:** The consultation paper mentions that such sale, disposal or lease happens either through Scheme of Arrangement or through Business Transfer Agreement, and that there is presently no explicit framework for protecting the interest of minority shareholders in the context of Business Transfer Agreement. Accordingly, the consultation paper has made various proposals including mandatory disclosures of the objects and commercial rationale for such sale etc. and the requirement of majority of minority voting, in addition to an existing (Companies Act) special resolution requirement.
- 4. ‘Board Permanency’ at listed entities:** The consultation paper mentions that there are many cases of permanent seats on company boards and that “promoters hang on to their seats making it harder for investors to effect management change”; also, “there are instances of promoter directors continuing on the board even after substantial divestment of stake and after ceding the control of the company”. In this context, the board proposes the need for introducing periodic shareholder approval requirements for all categories of listed companies and has also proposed a glide path to achieve that objective.

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7. RBI: FAQs on Digital Lending Guidelines

In continuation of the Guidelines on Digital Lending issued date September 2, 2022, RBI has issued FAQs on February 14, 2023. It aims at preventing exorbitant interest rates and increased accountability and also keeping a check on unethical loan recovery practices.

The FAQs deal with specific situations such as co-lending and loan of employee paid by employer's bank account. It is clarified that payment aggregators not providing lending service will not be governed by the guidelines.

8. Gujarat High Court: Stamp duty for merger of unlisted companies to be based on value of shares¹⁴

The Hon'ble Gujarat High Court in context of the Gujarat Stamp Act, 1958, held that the state can levy stamp duty in the event of amalgamation or reconstruction of unlisted companies based on their market value. The market value of shares will be deemed to be the face value as stated in Explanation III(c) of Article 20(d) of Gujarat Stamp Act, 1958, and share premium cannot be part of face value or the additional consideration. Further, the stamp duty cannot be charged by treating each amalgamation or reconstruction under a composite scheme as a separate transaction.

D. Goods and Service Tax Highlights

1. No GST is payable on supply of 'vouchers'¹⁵

The assessee is engaged in transactions of procuring Pre-paid Payment Instruments ('PPI') of Gift Vouchers, Cash Back Vouchers and E-Vouchers from the issuers and supplying them to its clients for specified face value who in turn issues such vouchers to their employees. With respect to the taxability of these vouchers, the Karnataka High Court quashed the ruling of AAR and AAAR and held that vouchers are PPI and their value accepted as consideration for supply of goods or services and they have no inherent value of their own. Also, the Hon'ble High Court clarified that the voucher will fall under the definition of money which is not covered within the scope of definition of goods and services. Therefore, no GST is payable on supply of vouchers.

Katalyst comments:

The Tamil Nadu AAAR in Kalyan Jewellers India Ltd [TS-131-AAAR(TN)-2021-GST] has held that 'Vouchers/PPIs/Gift cards' per se are neither goods nor services but are "means/instrument for payment of consideration".

2. Writ petition allowed where show cause notice is an order in itself¹⁶

The assessee received a show-cause notice ('SCN') regarding classification of product. The assessee filed a writ petition against the SCN, contending that it is pre-mediated. However,

¹⁴ Ambuja Cements Ltd v Chief Controlling Revenue Authority, Gujarat High Court, dated February 10, 2023

¹⁵ Premier Sales Promotion Pvt Ltd vs UOI & ors [TS-23-HC(KAR)-2023-GST]

¹⁶ Joyous Blocks & Panels Pvt Ltd vs. Assistant Commissioner [TS-727-HC(CAL)-2022-GST]

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the single bench of Calcutta High Court in the matter held that a writ petition against an SCN is not maintainable.

On intra-court appeal, the division bench of Calcutta High Court held that if the SCN suffers from lack of jurisdiction and is an order by itself, then courts can interfere by way of a writ. The Hon'ble High Court quashed the decision of the learned single bench and SCN due to the fact that the manner in which the authority had proceeded to issue the SCN didn't satisfy legal requirements and remanded the matter with a direction to issue fresh SCN with an open mind without pre-deciding any issue and give adequate opportunity to the assessee to submit its reply.

Katalyst comments:

A welcome decision by the division bench of Calcutta. Upon receipt of SCN, a writ petition can be filed if the SCN is an order by itself and pre-meditated.

3. Key recommendations of 49th GST Council meeting

Following are the key recommendations as discussed in the 49th GST Council meeting held in New Delhi on February 18, 2023:

- **GST compensation to States:** The Government to clear the pending balance of GST compensation of INR 16,982 crores for June 2022 to 23 States of India.
- **GST Appellate Tribunal:** The Council adopted the report of the Group of Ministers on the GST Appellate Tribunal with certain modifications. The final draft amendments to the GST laws shall be circulated to Members for their comments. The Chairperson has been authorized to finalize the same.
- **Amnesty scheme for pending GST returns:** Amnesty schemes have also been proposed for pending returns in FORM GSTR-4, FORM GSTR-9, and FORM GSTR-10, with conditional waiver or reduction of late fee.
- **Place of supply of services of transportation of goods:** The Council recommended rationalizing the provision of place of supply for services of transportation of goods by deletion of section 13(9) of IGST Act, 2017, so as to provide that the place of supply of services of transportation of goods, in cases where the location of the supplier of services or location of the recipient of services is outside India, shall be the location of the recipient of services.
- **Assessment of returns:** To enable the withdrawal of best judgment assessment orders, the time period for filing relevant returns to be increased from 30 days to 60 days, with an option for a further extension of up to 60 days, subject to certain conditions. An amnesty scheme has also been proposed for conditional deemed withdrawal of assessment orders in past cases.
- **Rationalization of late fees:** The Council has recommended rationalizing the late fee for delayed filing of annual returns in FORM GSTR-9 for registered persons with an aggregate

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turnover of up to Rs. 20 crores, with the late fee being reduced to Rs 50 per day for those with a turnover of up to Rs. 5 crores and Rs 100 per day for those with a turnover of more than Rs. 5 crores and up to Rs. 20 crores.

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