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Katalyst Kaleidoscope

February 2020: Tax and Regulatory Insights

A. Income-tax Highlights

1. Mumbai ITAT allows depreciation claim on goodwill arising out of payment made under a Business Transfer Agreement[1]

Tam Media Research Pvt Ltd ("the assessee") acquired the 'Adex Business' along with its assets and liabilities from M/s A C Nielson ORG-Marg Research Pvt Ltd for a total consideration of INR 12 Crores by way of a 'Business Transfer Agreement'. Accordingly, an amount in excess of the net assets acquired, INR 11.5 Crores, was capitalized in the books of assessee as goodwill on which depreciation was claimed.

The Hon'ble ITAT held that depreciation claimed on such goodwill falls within the four corners of the law laid down by the Hon'ble Supreme Court ('SC') in case of **Smifs Securities** and therefore is allowable as deduction against the taxable income.

Katalyst Comments: *The ITAT's decision allows acquirer's claim of depreciation on goodwill on businesses acquired under a Business Transfer Agreement, as the same is in line with the SC's decision in case of Smifs Securities. This decision yet again affirms the substance over form argument wherein the commercial nature of the transaction has been looked at, regardless of the tax benefit involved. From an IndAS perspective, the Acquirer Entity may further be required to attribute and allocate a portion of goodwill to particular intangibles (say, customer lists, know-how, etc.) at the time of acquisition; such attribution may further lead to a charge in the books in the form of amortization which the unallocated portion (in the form of residual goodwill) would not be subject to book amortization.*

2. Mumbai ITAT allows long-term capital loss on capital reduction; distinguishes Bennett Coleman SB-ruling[2]

The appellant, a US Entity being the holding entity of the Indian company whose shares were cancelled, claimed a long-term capital loss on capital reduction. Out of the total consideration of INR 39.99 crores, INR 10.33 crores being consideration to the extent of accumulated profits, was considered as deemed dividend. The balance consideration of INR 29.66 crores was appropriated towards sale consideration of shares and capital loss was determined accordingly.

The ITAT held that reduction of capital had resulted in "extinguishment of rights in shares‟ and that the definition of "transfer‟ u/s 2(47) of the Act includes "extinguishment of any rights‟ in a capital asset. Further, consideration pursuant to the capital reduction was duly received by the

[1] Tam Media Research Pvt Ltd vs ITO (ITA no. 6035/Mum/2009) (Mumbai ITAT) 10th Jan, 2020

[2] Carestream Health INC vs DCIT [TS-75-ITAT-2020(Mum)]

assessee. Therefore, the loss arising to the assessee on reduction should be allowed as a long-term capital loss eligible to be carried forward to subsequent years.

Katalyst Comments: *ITAT distinguished the Mumbai Special Bench decision in the Bennett Coleman case*[3] *wherein there was no change in the shareholding before or after the capital reduction (owing to capital reduction on account of reduction in face value) and there was no consideration which was received by the shareholder; therefore, such capital reduction was not construed to be "transfer" and hence, loss was not allowed basis the fact pattern that there was no receipt of consideration and that there was a mere substitution of one kind of share capital with another. On the other hand, the Carestream decision highlights that capital reduction which is on account of actual cancellation of shares and where consideration was involved, amounts to transfer of a capital asset and the resultant implications would follow. Given the decision of the Supreme Court in the case of Kartikeya v. Sarabhai v/s CIT*[4]*, capital loss on account of capital reduction by way of actual cancellation of shares and for which no consideration is paid (say, owing to accumulated losses) should also be permitted to be allowed for set-off/ carry forward, as the case may be.*

3. **Delhi ITAT deletes addition made u/s 56(2)(viib) -"excessive" share premium basis subsequent transfer of shares to a foreign buyer at much higher value**[5]

In case of Clearview Healthcare Pvt Ltd ('assessee' or 'company'), shares were issued at a premium of INR 150 per share during AY 2014-15 to resident shareholders (Face value being INR 10). The Assessing Officer, during the course of assessment proceedings, while determining the valuation of shares in accordance with the provisions of Rule 11UA, restricted the valuation of share at INR 144 per share and therefore held that the shares were issued at an "excess" share premium of INR 6 per share. The alleged excess premium was taxed in the hands of company u/s 56(2)(viib) of the Income-tax Act, 1961 ('ITA').

The Delhi Tribunal ('ITAT'), taking cognizance of the fact that the shares were ultimately bought by a foreign buyer on the basis of a detailed due diligence held that it cannot be said that subsequent money by foreign buyer to shareholder that were sellers in India who had subscribed the shares at a premium in the subject period was "unaccounted money". The ITAT further concluded that, in the absence of a case of revenue that the share premium received was not clean money and the company received unaccounted money disguised as share premium, held that the provisions of section 56(2)(viib) cannot be made applicable.

Katalyst Comments*: The decision of ITAT brings some respite in cases where, following a literal interpretation of the provisions of section 56(2)(viib) would have been prejudicial in cases of*

[3] Benett Coleman & Co. Ltd. V. ACIT [TS-580-ITAT-2011(Mum)]
[4] Kartikeya v. Sarabhai v/s CIT (228 ITR 163)
[5] M/s Clearview Healthcare Pvt Ltd Vs ITO (ITA no. 2222/Del/2019) (Delhi ITAT) (3rd Jan, 2020)

genuine transactions. Evolution of jurisprudence on this section needs to be seen vis-à-vis Section 68 (cash credits) of the ITA and presumably the jurisprudence like the above would make the interpretation of the section more logical by giving effect to the section keeping also in mind the context of section 68.

4. Delhi ITAT holds disbursement to holding company as income diversion by overriding title, and not a sham transaction[6]

In the case of Emmar MGF Construction Pvt Ltd ("the assessee"), a collaboration agreement was executed between assessee and its holding company, wherein 25% of the gross revenue out of the project undertaken by the parties to the agreement would go to the holding company for the risks assumed by the holding company. In addition to this, a separate arrangement was entered into between the two companies, wherein the holding company funded the assessee, for the purpose of execution of the said project, at an interest rate lower than that prevailing in the market.

The Assessing Officer held this as a sham arrangement by which the assessee reduced its tax liability by not offering the said 25% as its revenue, rather shifting it to the holding company, which already had brought forward losses.

The ITAT held that this is a case of diversion of income by overriding title where the holding company is paid, directly from the income source, for the risks assumed by it, by financing and providing guarantees, assuming commercial risks like delay in completion of the project, drop in sales, etc. ITAT held that assessee was under an obligation by virtue of the agreement to divert the income at source and also for the contributions made by the holding company. Just because the income is collected by assessee itself for or on behalf of the beneficiary, it cannot be inferred that it was only an application and not diversion. ITAT held that the collaboration agreement cannot be treated as a sham arrangement, taking into consideration the entire facts of the case, especially the contributions made by the holding company.

Katalyst Comments*: Diversion of income overriding title vs application of income is an established concept that has been approved by the Supreme Court in the case of Sitaldas Tirathdas[7] which held that there is a difference between an amount which a person is obliged to apply out of his income and an amount which by the nature of the obligation cannot be said to be a part of the income. Where the income is diverted before it reaches the assessee, it is deductible; but where the income is required to be applied to discharge an obligation after such income reaches the assessee, the same consequence, in law, does not follow.*

[6] Emmar MGF Construction Pvt Ltd (ITA no. 1731/Del/2014 & ITA no. 2001/Del/2014) 26th Dec, 2019

[7] **[**1961] 41 ITR 367 (SC) SUPREME COURT OF INDIA CIT v. Sitaldas Tirathdas

The Tribunal decision is in line with the principle that all arrangements that result in tax savings are not sham arrangements, merely because they result in tax savings and that the conclusion of whether it is a sham will depend on facts and not solely on resultant savings.

5. **Kolkata ITAT deletes addition under the head Capital gains in the case of conversion of sole proprietorship into a private limited company[8]**

The sole proprietor business of Mr. Ravi Jalan ('assessee') was converted into private limited company, wherein all the assets and liabilities of assessee were vested with the newly formed company. The consideration was paid by the company partly in form of shares and partly in cash thereby violating the last condition prescribed u/s 47(xiv) of ITA i.e. the sole proprietor receives consideration in form of shares only. The AO held that the transaction would be taxed under 'capital gains' and valued the shares at the Fair Market Value ('FMV") considering subsequent issue of shares at premium. The increased FMV, thus led to substantial tax demand in the hands of the assessee. The Assessing Officer, in addition to levying tax u/s 47A read with 47(xiv), also taxed under Income from other sources u/s 56(2)(vii)(c), since the value at which shares had been issued to the assessee was much lesser than the FMV.

The ITAT, relying on the decision of M/s Aravali Polymers LLP[9] held that though the violation of last condition of section 47(xiv) makes the transaction liable to tax under capital gains, the full value of consideration equals the cost of acquisition of net assets to the company which results in zero capital gains. The ITAT further held that subsequent issue of shares at a premium cannot be considered for the purpose of valuation of shares issued earlier, pursuant to the conversion of sole proprietorship business into a private limited company.

Katalyst Comments: *The ITAT has upheld the assessee's contention, on facts, and held that a subsequent transaction cannot impact an earlier transaction, and that the two are separate for determining assessee's tax liability. This principle can be useful in appropriate cases.*

6. **Kerala High Court holds that circulars issued by department cannot have primacy over binding decisions of jurisdictional High Court[10]**

While dealing with an issue relating to the deduction availed by co-operative societies u/s 80P of the ITA, the Kerala High Court ('HC') observed that once a superior forum (in this case, the High Court), has held stating that the Assessing Officer is not bound to allow a deduction under the relevant applicable provisions of the ITA regardless of a favorable CBDT Circular. It was held that, the criteria laid down by the departmental circular shall be disregarded, to the extent of the law laid down by the High Court.

[8] Shri Ravi Jalan Vs ITO (ITA 2292/Kol/2017) (Kolkata ITAT) 15th Jan, 2020
[9] M/s Aravali Polymers LLP Vs JCIT (Kolkata ITAT) order dt. 27th June, 2014
[10] Kuthannur Service Co-operative Bank Limited Vs ITO (ITA no. 197 of 2019) (Ker HC) (8th January, 2020)

The High Court held that clarificatory circulars issued for the guidance of the officers bind the Income Tax Authorities but not the High Court in interpretation of statutory provisions, and that "once a provision has been interpreted by the Superior Court, then it will not be open to the assessee to project an interpretation on the concerned provision which is in lines with the circular, but against the law laid down by the Court".

Katalyst Comments: *The High Court has laid down a principle that though departmental circulars / instructions are binding on the revenue authorities, wherever they are contrary to the law laid down by the jurisdictional High Court, the law as laid down by the Court should prevail. This can work both ways in the sense that "favorable" CBDT circular can be overturned by a court judgement.*

7. Delhi ITAT holds that the DTAA exempt income shall not be entitled to be excluded from 'book profits' under MAT provisions[11]

IRCON International Limited ('the company') has had incomes arising in various countries with which India has a Double Tax Avoidance Agreement ("DTAA"). While computing its income, the company excluded such income earned from its projects in Bangladesh, Malaysia & UK. The income was computed under the MAT provisions as the same had been applicable in the case of the company for the relevant assessment year. It would be noteworthy to observe that in case of the assessee in the previous assessment years, the concept of not including incomes exempt by virtue of DTAAs in computing the total income under MAT provisions, was not challenged. The Assessing Officer however, not having regard to this earlier position, added the same to the income of the company.

The Hon'ble ITAT held that while computing the income under the MAT provisions, the ITA provisions prescribe a specified list of additions/ deductions to be made in order to arrive at the book profits. The incomes being exempt by virtue of the provisions of the applicable DTAAs are not prescribed in the list of additions and subtractions. The exclusion of income is nowhere provided in the ITA and therefore it warrants adjustment to the computation of book profits liable for MAT. If it were the intention of the legislature to provide reduction in respect of such incomes, it would have been specifically provided so.

Katalyst Comments *MAT provisions are anyway not applicable where the company opts for reduced tax rates foregoing the deduction prescribed by the Taxation Laws (Amendment) Act, 2019. However, this will impact past situations, as well as those corporates not opting for the lower corporate tax rate. This ruling is one wherein the principal question is whether the income being outside the scope of total income under the ITA can be brought to tax indirectly through MAT*

[11] IRCON International Limited Vs DCIT (ITA no. 977/Del/2010 & 2220/Del/2011) (Delhi ITAT) 30th January, 2020

provisions. The judicial position is currently divided and not conclusive. For example, in the case of JSW Steel Limited v. ACIT[12], the Mumbai ITAT had held that capital surplus on account of write-back of loans, albeit credited to the P&L account, would not be subject to MAT since the original write back was itself not subject to tax under the normal provisions of income-tax.

8. Bangalore ITAT grants exemption u/s 10(23FB) to Venture Capital Fund on sale of listed shares of Venture Capital undertaking[13]

In case of True North Fund IIIA ('Venture Capital Fund' or 'assessee'), the shares held by the Venture capital fund in a Venture Capital Undertaking ('VCU') got listed consequent upon the amalgamation of the VCU with a listed entity. The AO held that since the shares sold by assessee were listed on a recognized stock exchange, an exemption u/s 10(23FB) cannot be allowed.

The ITAT held that the exemption condition to the effect that the shares of the VCU should not have been listed on a recognized stock exchange shall apply only at the time of making an investment. Referring to Regulation 12(d) of Venture Capital Fund regulations, ITAT held that the regulations itself visualize listing of shares in the future (clause (d) allows not more than 33.33% of the investible funds to be invested by way of IPO of VCU, debt instrument of VCU, preferential allotment of equity shares of listed entity, etc.), and thus subsequent listing of shares should not be a hindrance for availing an exemption u/s 10(23FB) of the ITA.

Katalyst Comments: *This decision brings relief to various funds where the investments were made when the VCU was an unlisted entity which got subsequently listed, being one of the common avenues for VCFs to seek exit.*

9. Introduction of Direct Tax Vivaad se Vishwas Bill, 2020 – Settling Direct tax disputes

The Union Budget referred to amounts tied up in litigation and dispute resolution being crucial; accordingly, a scheme called Vivaad se Vishwas ('VSV') scheme had been announced, but the final details of the scheme were to be notified. Following are the key highlights of VSV as now proposed:

- As of 30th November 2019, the amount of disputed direct tax arrears is INR 9.3 lacs crore and the actual collection in the FY 2018-2019 was INR 11.4 Lacs crore; accordingly, disputed tax arrears constitute almost 1 years' direct tax collection. Such litigation consumes copious amount of time, energy and resources of the Government, as well as of tax payers. It is in this context that the VSV scheme has been announced/amended.

[12] JSW Steel Limited v. ACIT (ITA No. 923/Bang/ 2009)
[13] ITO Vs True North Fund IIIA (ITA no. 486/Bang/2019) (Bangalore ITAT) 29th January 2020

- The scheme provides for payment by 31st March 2020 of the disputed tax and waiver of interest and penalty related thereto. There is also an option to opt for the scheme for penalty interest etc.; the table below explains the position:

	In case of payments made up to 31st March, 2020	**In case of payments made after 31st March, 2020**
Appeals filed by the assessee		
Other than search cases involving disputes relating to tax, interest Penalty, etc.	• 100% of the disputed tax; • Penalty and Interest would be waived	• 110% of the disputed tax; • Penalty and Interest would be waived
Where disputes relate to only interest, penalty or levy	• 25% of the disputed interest, penalty or levy; • Balance 75% would be waived	• 30% of the disputed interest, penalty or levy; • Balance 70% would be waived
Appeals filed by the Revenue Department/Revenue Department has lost an issue		
Other than search cases involving disputes relating to tax, interest Penalty, etc.	• 50% of the disputed tax; • Penalty and Interest would be waived	• 55% of the disputed tax; • Penalty and Interest would be waived
Where disputes relate to only interest, penalty or levy	• 12.5% of the disputed interest, penalty or levy; • Balance 87.5% would be waived	• 15% of the disputed interest, penalty or levy; • Balance 85% would be waived

- The revised Scheme provides that filing of declaration will not set any precedent and it cannot be claimed in any other proceedings that the taxpayer or the Department has conceded its tax position by settling the dispute

- Though the revised Scheme does not allow filing declaration issue wise (it is not possible for declarant to file declaration for some issues and litigate the balance issues), it provides that in a case where the taxpayer has got a favorable decision on an issue at higher forum, he would be required to pay only 50% of disputed tax on that issue even in the cases in which he has filed appeal.

B. Corporate Law Highlights and Insolvency and Bankruptcy Code

1. Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2020[14] for takeover by members of unlisted companies

Section 232 of the Companies Act, 2013 deals with compromise and arrangements, including mergers and demergers. Section 230(11) provides that any compromise or arrangement may include a takeover offer made "in such manner as may be prescribed". The proviso to section 230(11) deals with listed companies, wherein the takeover is required to be as per the SEBI takeover regulations.

This has now been extended to private and unlisted companies as well vide a notification dated 3rd February 2020 has been issued by the Ministry of Corporate Affairs inserting Sub-rule (5) in Rule 3 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 and the gist is as under:

- A member of a company may make an application for arrangement for the purpose of takeover offer, wherein such member, along with any other member, holds not less than 75% of the shares in the company and such application has been filed for acquiring any part of the remaining shares of the company.

- Such application shall contain a report of a registered valuer disclosing the details of the valuation of the shares proposed to be acquired, taking into account the highest transacted price during the preceding 12 months and the fair price of the shares is to be determined by the registered valuer. The application shall also contain details of the bank account, wherein a sum of not less than 50% of the total consideration of the takeover offer is deposited.

Katalyst Comments: *The provision appears to be a squeeze out provision for the minority shareholders of unlisted companies. However, it is circumscribed by valuation safeguards from the perspective of minority shareholders. The concept of the applicant acting in concert with those holding (along with him) 75% of the value of shares, is not expressly brought out. Further, the provision requiring deposit of 50% of the amount is fairly cumbersome. Also, the regulations do not provide the time limit by which the amount is to be deposited (presumably before the application), the duration for which the amount shall remain deposited, whether it can be an interest-bearing account and other related factors.*

[14] MCA notification dated 3rd February, 2020

2. MCA issues Companies (Winding Up) Rules,2020

MCA has issued The Companies (Winding Up) Rules, 2020[15] comprising of 191 rules and 95 forms, effective from 1st April, 2020, applicable for winding up of companies under the Companies Act, 2013.

Key features:

- The petition for winding up of a company shall be presented in the prescribed Forms and such petition shall be verified by an affidavit made by the petitioner. The statement of affairs, to be filed in the form prescribed and shall contain information updated less than 30 days prior to the date of filing the petition.

- These rules shall be applicable to all types of liquidators unless specified.

- The order for winding up shall be in the format prescribed and it shall be sent by the Registrar after it is signed and sealed within a period not exceeding 7 days from the date of receipt of the order by the Registrar, to the Company Liquidator and the Registrar of Companies. Certain forms have been prescribed for this as well.

- The Companies (Winding Up) Rules 2020 further provide rules for Application for stay of suits etc. on winding up order, Report by Company Liquidator, Settlement of list of contributors, Advisory Committee, Registration and Books of Account to be Maintained by Company Liquidators, Collection and Distribution of Assets in Winding up by Tribunal, Calls in Winding up by Tribunal, Dividends and Returns of Capital in Winding up by Tribunal, Termination of Winding up, Payment of Unclaimed Dividends or Distribution of Assets, Summary Procedure for Liquidation etc.

Katalyst Comments: *Companies intending to wind up voluntarily or for grounds other than inability to pay debts, can now make an application under the Companies Act, 2013. The rules notified provide a structured and time bound process of winding up of company. The summary procedure of liquidation is that the Central government will provide required approvals to such companies for the normal winding up process which is otherwise undertaken through the tribunal, thereby shortening the winding up timelines. This is also likely to help lenders/ banks to achieve faster recovery in situations where they have taken over the control of the Company or invoked pledge.*

3. Committee constituted for recommending rules & regulatory framework for smooth implementation of proposed Cross Border Insolvency provisions

[15] MCA Notification dt. 24th January, 2020.

The Ministry of Corporate Affairs ("MCA") has, *vide* a notification[16] constituted a Committee to suggest its recommendations on rules & regulatory framework for smooth implementation of the proposed Cross Border Insolvency provisions under the Insolvency & Bankruptcy Code, 2016.

The Committee is constituted for the purpose of studying and analyzing the recommendations earlier made by the Insolvency Law Committee (ILC) in its Report on cross border insolvency; by adopting the United Nations Commission on International Trade Law ('UNCITRAL') Model Law in India with some modifications and carve outs suggested therein, and shall submit its report within 3 months.

4. NCLAT rejects scheme in absence of correct methodology to determine the share exchange ratio pertaining to a scheme of amalgamation.[17]

In a petition filed for sanctioning scheme of amalgamation between transferor and transferee companies, the NCLAT noted that the valuation of each share was not performed by the valuer and thereby, the share exchange ratio arrived at could not be relied upon. The NCLAT further stated that the share exchange ratio had to be an outcome of the share value determined for an individual company to ensure that the exchange ratio is fair. As the report was devoid of necessary details, the credibility of the exchange ratio was at best termed as guess work by the valuer and the scheme was therefore rejected.

5. NCLAT holds Insolvency to be limited to 'a real estate project' and not 'a real estate firm'[18]

The National Company Law Appellate Tribunal (NCLAT),[19] held that any insolvency process initiated by a flat buyer or financial institution would be limited to the project concerned only and not impact other projects of the same developer.

The NCLAT bench headed by Chairperson Justice S J Mukhopadhaya opined that the entire insolvency process initiated over the plea of either a flat buyer or bank or any other financial institution would be limited to the concerned project only and the same cannot be clubbed with the other projects of the same developer.

The Appellate Tribunal was of the view that that there should be a "reverse corporate insolvency resolution process" wherein the insolvency process is initiated against a real estate company, no home buyer can approach the National Company Law Tribunal (NCLT) or the NCLAT to seek refunds for the project. In case the flat owners of such projects wish to seek a refund for the particular

[16] MCA notification dated 23rd January, 2020
[17] Ankit Mittal vs Ankita Pratisthan Ltd. (113 taxmann.com 294) NCL-AT (2020)
[18] Company Appeal (AT) (Insolvency) No. 926 of 20191
[19] Order dated 4th February in the case of *Flat Buyers Association Winter Hills – 77, Gurgaon vs Umang Realtech Pvt. Ltd*

project of the real estate company which is undergoing insolvency, they are open to sign an agreement, either with the interim resolution professional, or the promoter to find a new buyer and get the money back if and when that flat is sold.

Katalyst Comments: *The above order secures other projects of a particular developer which may be near completion or can be completed and paves way for completion of the homebuyer's project without affecting the other projects. However, the other industry opinion that the order may create more chaos than good and that it is contrary to the fundamentals of the insolvency law cannot be ignored.*

6. New Web Form for Company incorporation[20] – A step towards ease of doing business

- As a part of Government of India's ease of doing business initiatives, MCA would be shortly deploying and notifying a new Web form "SPICe+" replacing the existing SPICe form.
- This would act as an integrated platform that shall offer multiple services like name reservation, incorporation, DIN allotment, mandatory PAN issue, TAN, EPFO, ESIC, Profession tax registration and opening of a bank account.
- Post notification, name reservation & incorporation should be through the new form only.

C. RBI and Foreign Exchange Regulations Highlights

1. Reserve Bank of India ("RBI") reopens allotment of investment limit under the revised Voluntary Retention Route ("VRR") for investments by Foreign Portfolio Investors ("FPIs")

RBI had introduced VRR for investments by FPIs in March 2019, to enable the FPIs to invest in debt markets in India. As on 31st December, 2019, around INR 54,300 crores had already been invested, out of the INR 75,000 crores offered for investment. Basis the traction garnered, on 23rd January, 2020 RBI has notified a revised scheme for allotment from 24th January, 2020 with the following features:

- The investment cap is increased to INR 1,50,000 Crores from INR 75,000 Crores.
- FPIs that have been allotted investment limits under VRR may, at their discretion, transfer their investments made under the General Investment Limit to VRR.
- FPIs are also allowed to invest in Exchange Traded Funds that invest only in debt instruments.

[20] As per the messaged displayed on the MCA website

<u>Katalyst Comments:</u> *The amendment allows FPIs to invest in securities governed by the recently notified Foreign Exchange Management (Debt Instruments) Regulations, 2019 notified vide Notification No. FEMA.396/2019-RB dated October 17, 2019. The amendment helps achieve certain operational flexibilities as to transfer of general investment limit to VRR, investments in ETFs, etc.*

2. RBI increases the short-term investment limit for FPIs in Government Securities, Corporate Bonds

The RBI has amended its directions[21] pertaining to investment by FPIs in Debt. As per the erstwhile directions, short term investments by an FPI could not exceed 20% of the total investment of FPI in either Central Government Securities (including treasury bills) or State Development Loans, Corporate Bonds. This limit has now been increased to 30%.

Further, investments in security receipts are currently exempted from the short-term investment limit. By bringing in this circular, the RBI has extended the exemption for FPI investments in Debt instruments issued by Asset Reconstruction Companies; and Debt instruments issued by entity under the Corporate Insolvency Resolution Process through the resolution plan of Insolvency and Bankruptcy Code, 2016.

3. RBI revises guidelines for deferment of date of commencement of commercial operations ("DCCO") in relation to advances pertaining to commercial real estate and non-infrastructure projects under implementation

The RBI, vide its updated circular[22], and in furtherance of its circular dated 6th April, 2015[23], has revised the guidelines for deferment of Date of commencement of Commercial Operations ('DCCO') in order to harmonize the guidelines for deferment of date of commencement of commercial operations (DCCO) for projects in non-infrastructure and commercial real estate (CRE) sectors.

As per the said circular, revision of DCCO and consequential shift in repayment schedule for equal or shorter duration (including the start date and end date of revised repayment schedule) will not be treated as restructuring, provided that the revised DCCO falls within one year from the original DCCO stipulated at the time of financial closure for CRE projects.

In case of CRE projects delayed for reasons beyond control of the Promoter, banks may restructure them by way of revision of DCCO up to another one year and retain 'standard asset' classification

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[21] AP (DIR Series) Circular no. 18, dated 23rd January, 2020
[22] RBI Circular dated 7th February, 2020
[23] DBR no. BP.BC.84/21.04.048/2014-15

if the account continues to be serviced. Thus, property developers will have an additional year to address their funding issues before the banks have to classify a loan as restructured.

Katalyst comments: *With this extension, real estate developers will now be able to make modifications to their repayment schedule, which will result in more liquidity as project cash flows will not be utilised for service of debt (for one year) but for completion of the project. This is complementary to the INR 25,000 Crore stressed asset fund announced by the Government earlier.*

D. Securities and Exchange Board of India ("SEBI")

1. Recommendations of the Working Group on Related Party Transactions ("RPT")

SEBI constituted a working group in November 2019 to review the policy pertaining to Related Party Transactions ('RPT') under the chairmanship of Mr. Ramesh Srinivasan, Managing Director and CEO of Kotak Mahindra Capital Company. The terms of reference of the Working Group were to make recommendations to SEBI vis-a-vis policy relating to RPT including definitions, threshold and approval process and various other matters related thereto. The working group submitted its report 22nd January, 2020 and comments are invited on the report by 26th February, 2020.

The Working Group has mentioned that one commonality in major corporate wrongdoings was that they were allegedly carried out by persons with an ability to influence the company and also that companies appear to have diluted or circumvented RPT approvals etc. for continuous lending to group companies.

The Working Group has made several recommendations[24], some of them have been captured below:

- Broad basing the definition of 'related party' by recommending that, the requirement of holding 20% or more by the promoter or promoter group in a listed entity should be done away with.

- In terms of definition of related party transactions, the recommendation is again to make the definition an all-inclusive one by bringing under its ambit transactions that are carried out by subsidiaries of listed entities. Also, clarificatory amendments have been suggested to the effect that issues of specified securities on preferential basis (subject to SEBI ICDR requirement) and corporate actions like payments of dividend and buyback should not be covered by RPT definition.

[24] Report issued on 27th January, 2020/

The threshold for approval of RPT is sought to be reduced to INR 1,000 Crs. or 5% of annual total revenues, total assets or net worth of the listed company on a consolidated basis, whichever is lower.

- A new sub-regulation has been introduced wherein the information to be provided to the shareholders is proposed to be made more exhaustive in terms of prescribing information requirements for notices sent to shareholders for seeking approval, including whether the approval by the audit committee was unanimous or not; also, the valuation or other external reports, if any, obtained by the listed entity in relation to the proposed transaction would be made available for inspection.

- Insofar as the mandatory review by the audit committee in case of related party transactions are concerned, the LODR is recommended to be modified for the audit committee to mandatorily review a prescribed list of information, including the tenure and value of the proposed related party transaction and several other items of information if the transaction relates to loans or advances Additionally, the status of long term (more than 1 year) or recurring related party transactions on an annual basis shall be provided to the Audit Committee.

Katalyst comments: *Though the recommendations appear to be making the regulations cumbersome, they may be effective in plugging some gaps. However, regulatory provisions are becoming very restrictive and compliance based, thereby significantly impacting ease of doing business.*

2. SEBI issues interpretative letter stating the definition of "net worth" specified under the Companies Act, 2013 would be considered to determine material subsidiaries

SEBI has by way of an Interpretative Letter in response to[25]Informal Guidance sought by AGC Networks Limited, addressed the issue of determining the net worth for classifying subsidiaries as material subsidiaries. Regulation 24 read with Regulation 16 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR") require determination of material subsidiaries.

SEBI clarified that the word 'Net worth' has been defined in SEBI LODR under Regulation 2(1)(s) as "net worth defined under in sub-section (57) of section 2 of the Companies Act, 2013." Therefore, identification of the subsidiaries as material may be done in accordance with the definition of net worth as provided under the said section including the deductibles mentioned therein.

3. SEBI issues an interpretative letter stating Foreign Portfolio Investors ("FPIs") are not permitted to invest in unlisted equity shares of an Indian Company.

[25] SEBI/CFD/CMD2/TC/OW/P/2020/3207/1 dt. 24th January, 2020

SEBI considered this issue in an interpretive letter[26] issued by it to IPFII Singapore 4 Pte Ltd. The applicant intended to invest in one equity share of a private limited company and seek clarification on whether an FPI can invest in unlisted equity shares of an Indian Company.

SEBI clarified as under:

- Regulation 20(1)(a) of SEBI (Foreign Portfolio Investors) Regulations, 2014, ('FPI Regulations') specifies that an FPI can invest in shares, debentures and warrants issued by a body corporate listed or to be listed.

- Regulation 20(8) of the said Regulations permits investment by FPI as a person resident outside India in accordance with the provisions of the Foreign Exchange Management Act, 1999, rules and regulations made thereunder.

- The Foreign Exchange Management (Non-Debt Instruments) Rules, 2019, under clause 1(a) of Schedule II, permit FPIs to invest in equity instruments of an Indian company listed or to be listed on a recognized stock exchange in India, subject to conditions mentioned therein.

- Thus, as far as equity instruments are concerned, FPIs may only purchase or sell equity shares of Indian company listed or to be listed on any recognized stock exchange subject to conditions provided under applicable laws.

4. SEBI provides an interpretative letter on applicability of Share Based Employee Benefit Regulations, 2014 (SBEB Regulations) on SAR for benefit of employees of JVs and Promoter Controlled Entities[27]

JSW Steel Limited requested an informal guidance by SEBI in proposed scheme proposed, under which JSW Steel Limited intended to issue cash-based Stock Appreciation Rights ('SARs') linked to share of JSW Steel Limited to employees of Joint Ventures and Promoter controlled entities of the JSW group. The issue was to be made through a Trust established JSW entities which shall be managed by professional trustees appointed by JSW Entities.

SEBI, under its informal guidance, said that the provisions of SBEB regulations shall apply to those companies whose shares are listed on any recognized stock exchange in India and has a scheme, which is set up, funded or guaranteed and controlled and managed by the company or any other company in its group for the direct or indirect benefit of the employees.

[26] SEBI/HO/IMD/FIIC/OW/P/2020/3302/1 dated 24th January, 2020.
[27] Informal Guidance by SEBI dated 5th November 2019 as requested by JSW Steel Limited

SEBI has clarified that in case of employees of JVs (with less than 50% stake of the listed entity), the SEBI (Share Based Employee Benefits) Regulations, 2014 ("SBEB") shall not apply as the said Scheme is not for the benefit of the employees of the listed company or its holding company or its subsidiary company, as provided in Regulation 2(1)(f) of the SBEB Regulations. Further, the SBEB Regulations were also not applicable in case of promoter controlled entities (not falling within the definition of group entities), as the scheme is neither issued by the listed company or its group companies as required by Regulation 1(4), nor is it for the benefit of employees of the listed company or other companies included in Regulation 2(1)(f) of the SBEB Regulations.

Katalyst Comments: *The informal guidance is helpful in understanding SEBI's approach towards such schemes where JVs and other entities of the promoters are involved.*

5. **SEBI has notified Portfolio Managers Regulations, 2020, regulating the role of Portfolio Managers**

SEBI issued the Portfolio Managers Regulations by notification in the Official Gazette on 16th January 2020. A summary of certain key provisions is provided below:

Regulation	Existing Regulation	Modifications made	Katalyst Comments
23(2)	The ticket size for minimum investment per client was INR 25 Lakhs	The same has been amended and increased to be INR 50 Lakhs	Whilst a PMS is more sophisticated an investment as compared to Mutual Funds and although the intention has been to make the securities market in India more investor friendly, the doubling of ticket size may reduce the attractiveness of the PMS schemes to investors.
7(g), 9	The requirement of Net Worth for the Portfolio Managers was earlier INR 2 Crores	This has been revised upwards to be made into INR 5 Crores	Although the ultimate impact of increasing the net worth threshold is to eliminated the not serious players in the market, this could prove to be an outlier wherein several small players could face an issue

Regulation	Existing Regulation	Modifications made	Katalyst Comments
			in complying with the revised threshold.
24(4)	Portfolio Managers were not permitted to invest in unlisted securities	Portfolio Managers offering non-discretionary and advisory services to clients shall now be permitted to invest 25% of the Assets under Management in unlisted securities.	The spectrum of investments is now extended to unlisted securities as well so as to have a wider and more diverse investment portfolio. However, practically such non-discretionary schemes are very few.

6. **SEBI Issues guidelines for rights issue of units by listed REITs and InvIT**

SEBI issued a Circular[28] dated January 17th, 2020 providing guidelines for rights issue of units by listed REITs and InvITs. This circular lists down the conditions which need to be fulfilled and are as follows:

- A resolution of the Board of Directors of the manager/investment manager (as the case maybe) approving the rights issue in addition to in-principle approval of the stock exchange for listing;
- REITs/InvITs are barred from making a rights issue, in case their sponsor group or managers have fugitive economic offenders as their Promoters/Partners/Directors;
- The investment managers are inter alia required to (i) file the draft letter of offer with the stock exchange, (ii) decide the issue price before determining the record date, in consultation with the lead merchant banker, (iii) separately provide in annexure disclosures to be made in the draft letter of offer and letter of offer;
- Investment managers are mandated to announce the record date to stock exchange(s) at least 3 working days prior to the record date and requires rights issue to open within 3 months from the record date, which should be kept open for 3 - 15 working days;

[28] SEBI Circular SEBI/HO/DDHS/DDHS/CIR/P/2020/10 dt. 17th Janaury,2020.

- The manner of issuance and allotment of units, requires REITs and InvITs to file an allotment report with SEBI providing details of the allottees and allotment made within 15 days of the issue closing date has been outlined

7. Statement of Deviation / Variation in the use of Issue proceeds – SEBI Circular

As per the SEBI Listing Regulations (LODR), a listed entity is required to submit to the stock exchange, a statement indicating deviation or variation, if any, in the use of proceeds of issue of non-convertible debt securities (NCDs) or non-convertible redeemable preference shares (NCRPs). In this regard, vide a circular[29] , the SEBI has issued a Format for 'Statement indicating Deviation or Variation in the use of proceeds of issue of listed NCDs or NCRPs (Format / Statement).

The Format shall be applicable for funds raised by entities through issuance of listed NCDs or NCRPs. The said Statement shall be submitted to the Stock Exchange(s) on half yearly basis, within 45 days of end of the half year, until such funds are fully utilised or the purpose for which these proceeds were raised has been achieved.

E. Goods and Service Tax Highlights <<Pending>>

1. Interest payable on 'cash component' of tax remitted and not on 'ITC component'

The Madras High Court(HC)[30] has allowed the writ and held that interest u/s 50 of the CGST Act, 2017('CGST Act') is applicable on 'cash component' of tax remitted and not on the 'ITC component' as ITC is available all the while with the Department to the credit of assessee and the same is neither 'belated' or 'delayed'.

Katalyst Comments: *The ruling clarified the anomaly w.r.t. applicability of interest either on gross liability (including ITC) or on 'cash component'. Further, the Madras HC has also clarified that proviso to section 50 of the CGST Act regarding levy of interest on tax paid in 'cash' has been inserted with effect from 1st August, 2019, but clearly seeks to correct an anomaly in the provision as it existed prior to such insertion. Therefore, it should be read as clarificatory and operative retrospectively.*

2. 'Corpus contribution' by members/apartment owners to 'Residential Welfare Association' is liable to GST

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[29] SEBI Circular SEBI/HO/DDHS/08/2020 dt. 17th January,2020

[30] In the matter of Refex Industries Limited vs. Assistant Commissioner of CGST & Central Excise [TS-89-HC-2020(MAD)-NT]

Karnataka Appellate Authority of Advance Ruling('AAAR')[31] has modified the ruling of Advance Ruling Authority ('AAR') to the extent that 'corpus contribution' by members/apartment owners to 'Residential Welfare Association' is liable to GST. Further, AAAR held that meaning of service is to be taken from the recipient's point of view and accordingly, it can be said that any transaction which gives the recipient a benefit can be considered as a service. Also, the AAAR opined that SC ruling in Calcutta Club Ltd. rendered in context of service tax will not influence the determination of taxable event of 'supply' under GST.

Katalyst Comments: *This ruling does not appear to have considered the decision of Hon'ble SC in case of Calcullta Club Ltd regarding services provided by a club to its members. As such, the definition of 'consideration' provides that the deposit given in respect of the supply of goods or services or both shall not be considered as payment made for such supply unless the supplier applies such deposit as consideration for the said supply. The 'corpus' collected by the 'Residential Welfare Association' should have been treated as 'consideration' or 'advances' for future supply*

3. Gujarat HC[32] strikes down levy of IGST on ocean freight

Gujarat HC has held that no GST under RCM is payable by the importer on 'ocean freight' charged by the shipping line and held the levy unconstitutional. Further, the HC also held that when transportation of goods terminates in India, neither importer can be considered as 'service recipient' nor such supply of transportation of goods takes place in India.

Katalyst Comments: A *very important and welcome judgment,. the ambiguity regarding dual levy of GST on 'Ocean freight' has been clarified to a great extent.*

4. Valuation in case of supply to distinct person – Rules not be followed sequentially

The AAAR of Tamil Nadu[33] has held that Rule 28 of the CGST Rules, 2017 provides that in case of supply between distinct persons, the assessee has an option to adopt 90% of price charged to unrelated recipients as value to be adopted initially (first proviso) and alternatively, if full ITC is available to the recipient, the invoice value will be the 'Open Market Value' (second provis0). The AAAR was of the view that there is nothing in the Rule to show that second proviso is subordinate to the first proviso. It independently deals with a scenario where the recipient is eligible for full ITC.

Katalyst Comments: *The AAAR has clarified that second proviso to Rule 28 of CGST Rules does not restrict its application as in the first proviso, which is to be applied for cases of 'as such supply' only.*

[31] Vaishnavi Splendour Homeowners Association **[**TS-77-AAAR-2020-NT**]**
[32] Mohit Mineral Pvt. Ltd. [TS-29-HC-2020(GUJ)-NT]
[33] Specsmakers Opticians Private limited-[TS-1223-AAAR-2019-NT]

5. **No ITC on replacement of lift/elevator as it is an integral part of the building**

Maharashtra AAR[34] has held that lift is an integral part of the building (i.e. an immovable property) and hence, as per the restrictions for availment of ITC provided u/s 17(5) of the CGST Act, no ITC is available on replacement of lift/elevator to a GST registered Co-operative Housing Society.

6. **Govt. releases concept note & updated FAQs on 'E-invoice'**

Key features of the document:

- The flow of the e-invoice generation, registration and receipt of confirmation has been clarified
- E-invoice will not be generated at the GST portal, rather the invoice will be generated from the accounting system/ ERP or excel based tools or any such tools used by the taxpayer daily.
- Taxpayer/seller has to report the generation of invoice (i.e. JSON of the e-invoice) to the Invoice Registration Portal (IRP) of GST and IRP will generate a unique Invoice Reference Number (IRN).
- The IRP, upon receiving the confirmation from Central Registry, will add its signature on invoice data and generate a QR code to the JSON and send it back to the seller.
- The seller, post receipt of digitally signed JSON with IRN and QR code, will upload the invoice with GST and e-way bill system and the said data will be ultimately used for GST return preparation purpose
- The standard procedures to be adopted will ensure that the invoice shared by seller with his buyer or bank or agent or any other player in the whole eco-system can be read by machines and obviate data entry errors.

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[34] In the matter of Las Palmas Co-Operative Housing Society Limited- [TS-80-AAR-2020-NT]

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