KATALYST
ADVISORS LLP

Katalyst Kaleidoscope

May 2020: Tax and Regulatory Insights

A. Tax and regulatory aspects arising out of Covid-19 measures:

1. Economic stimulus in response to Covid-19

Pursuant to the announcement by the Prime Minister in his nation-wide address on May 12, 2020 regarding an economic stimulus of Rs. 20 lakh crores (including the already announced measures by the Ministry of Finance and the Reserve Bank of India), the Finance Minister announced five tranches of measures over five consecutive days starting May 13, 2020.

- While the announcements focused on reliefs to MSMEs, NBFCs, power distribution companies, contractors and real estate developers, they also covered sectors such as coal, minerals, defence production, airspace management and related areas, space and atomic energy. The final set of announcements covered reforms such as:

  Ease of doing business:
  - Permitting direct listing of securities by Indian public companies in foreign jurisdictions
  - Companies only listing Non-Convertible Debentures on stock exchanges not to be regarded as listed companies

  Decriminalization of Companies Act, 2013:
  - Several violations under Companies Act, 2013 involving technical and procedural defaults will be decriminalized
  - Compoundable offences will be shifted under internal adjudication mechanism and powers of Regional Director will be enhanced for compounding

  Insolvency and Bankruptcy Code:
  - Minimum threshold to initiate insolvency proceedings increased from INR 1 lakh to INR 1 Crore
  - Suspension of fresh initiation of insolvency proceedings up to one year

- Other measures include extension of due dates for filing of tax returns and tax audit reports, 25% reduction of rates at which tax is deducted or collected at source for various categories of payments (amounts paid or credited from 14 May 2020 till 31 March 2021). Key categories include:

Nature of payment (Section of Income-tax Act, 1961)	New rate (*erstwhile rate*) (%)
(i) Interest on securities (section 193)	7.5 (*10*)
(ii) Dividend (section 194)	7.5 (*10*)
(iii) Payments to contractors (section 194C)	1.5/ 0.75 for individual/ HUF (*2/ 1*)

Nature of payment (Section of Income-tax Act, 1961)	New rate (*erstwhile rate*) (%)
(iv) Rental payments (section 194-I)	7.5 for immovable property/ 1.5 for plant and machinery (*10/ 2*)
(v) Payment for Joint Development Agreements (section 194-IC)	7.5 (*10*)
(vi) Fees for professional and technical services	7.5/ 1.5 for managerial, technical, consulting services, certain royalty (*10/ 2*)

Katalyst comments: *While the economic package was supposedly to focus on land, liquidity, labour and laws, the measures only address some of the liquidity and labour issues, whereas the land and laws related measures are left badly wanting. Moreover, the sector-specific announcements also seem quite disconnected from the on-ground reality; several industries that have been severely impacted by the pandemic such as airlines, hospitality, retail and real estate have been left to fend for themselves.*

2. Recommendations in the "Fiscal Options and Response to COVID-19 Epidemic" (FORCE) report

In response to the impact of Covid-19 on the economy, a group of officers of the Indian Revenue Service prepared and submitted a report to the Central Board of Direct Taxes ('CBDT'), making recommendations to improve revenue collections. The report was also published publicly and created quite a furor in the taxpayer community.

Subsequently, the CBDT and Ministry of Finance clarified that no such report was sought from these officers and the views presented in the report did not reflect official policy of the government. While the report has been discarded, its key recommendations are tabulated below:

Objective	Suggested measures
Revenue mobilization (through additional tax burden)	• Higher tax for "super rich" by increasing tax rate applicable to the highest slab to 40% (effectively, translating into ~59% for highest income earners) • Introducing "Covid Relief Cess" @ 4% • Re-introduction of Wealth Tax on net wealth in excess of Rs 5 cr • Re-introduction of Inheritance Tax • Increasing surcharge on income of foreign companies have a presence in India • Introducing Base Erosion Anti-Abuse Tax on payments to foreign related parties in the nature of base-erosion (viz. interest, royalty, etc.) • Increasing rate of Equalisation Levy

Objective	Suggested measures
Revenue mobilization (other modes)	• Mobilising CSR funds by treating contribution to Chief Ministers' Relief Funds and PM CARES for corporate social responsibility purposes • Incentivising contribution to the PM CARES Fund • Introducing new tax savings scheme (such as NSC)
Taxpayer welfare	• Allowing set-off of short-term capital loss against salary income • Incentivising MSME by permitting carry back of losses up to 5 years • One-time reduction in tax rates for stressed sectors and additional depreciation to incentivize capital expenditure • 'Zero scrutiny year' and speedy processing of tax refunds

Katalyst comments: *Some of the propositions like carry back of losses are already in existence for several OECD countries such Singapore, UK, USA, Germany, etc. and should anyway be implemented. Whilst it is not an official CBDT/ Government report, the report does indicate the mindset of revenue officials and to that extent, is worrying. The need of the hour is to have a consultative process amongst all the stakeholders to, inter alia, simplify the law, have entity-restructuring facilitative provisions (such as continuity of business losses in these times), streamlining interpretations through CBDT circulars, etc. The world economy and the Indian economy is going through its most serious crisis ever, and the last thing one needs at this time is distractions of this nature.*

3. CBDT issues clarification with respect to determination of residential status for FY 2019-20[1]

Owing to the lockdown introduced for addressing Covid-19 in India, a number of individuals visiting India with the intention of leaving after a particular duration, thus ensuring that they maintain their status as a non-resident or a not ordinary resident during FY 2019-20, have been unable to return to their respective home countries.

So that such individuals do not get characterised as "resident" under section 6 of the Income Tax Act, 1961 ('Act') due to the inevitable prolonged stay, CBDT has issued the following clarification for the purpose of determining residential status for FY 2019-20 under section 6 of the Act in case of individuals who came to India for a visit before 22 March 2020:

- *If quarantined*: If the individual is quarantined in India on or after 1 March 2020, period of his stay from the date of his quarantine to 31 March 2020 (or up to his date of departure in case he departed on an evacuation flight on or before 31 March 2020) shall be excluded;

[1] CBDT Circular No. 11 of 2020 dt. May 8,2020

- *If not quarantined*: In any other case, the individual's period of stay in India from 22 March 2020 to 31 March 2020 (or up to his date of departure in case he departed on an evacuation flight on or before 31 March 2020) shall be excluded;

Katalyst comments*: This is a much-welcome and rational clarification, and considering the extension of lockdown beyond 31 March 2020 into the next year i.e. FY 2020-21, CBDT is expected to issue a similar circular for that year once the flight operations are resumed. However, international flights resumption from India is not the only aspect; the intended destination country also needs to open its borders. Hence, logically, the exclusion of the number of days stay in India should factor that aspect in, whilst issuing the order for calculation of the number of days stay in India.*

4. Other measures introduced in response to Covid-19

Particulars	Measures
Tax audit report - deferment of timelines in reporting certain clauses	CBDT has issued an order[2] stating that the reporting under clause 30C (GAAR reporting) and clause 44 (GST compliance) in Form 3CD will be kept in abeyance till 31 March 2021.
Extension of timelines for holding AGM	• MCA[3] permits companies with financial year ending on December 31, 2019 to conduct their AGM within a period of 9 months (instead of existing timeline of 6 months) from the closure of the financial year (i.e. by 30 September 2020). • Subsequent to the above relaxation by MCA, SEBI[4] also relaxed the timelines for top 100 listed entities by market capitalization whose financial year ended on December 31, 2019 for holding the AGM within a period of 9 months from the closure of the financial year.

B. Income-tax Highlights

1. Delhi ITAT upholds that transfers pursuant to family arrangement cannot be termed as gift/ benefit/ perquisite and cannot be taxed in the hands of a third party assessee (i.e. shareholder of recipient assessee company)[5]

The assessee, an investment company, had received shares of a few group companies without paying consideration as a part of internal family realignment. Pursuant to such transfer, shares of the recipient assessee company were gifted by the shareholder to a private trust.

[2] CBDT Circular No. 10 of 2020 dt. April 24,2020
[3] MCA General Circular No. 18/2020 dt. April 21, 2020
[4] SEBI/HO/CFD/CMD1/CIR/P/2020/71 dt. April 23, 2020
[5] Glebe Trading Pvt. Ltd [TS-230-ITAT-2020(DEL)]

The tax officer held that the receipt of shares by recipient company pursuant to internal family realignment amongst family members could not be regarded as a valid gift, considered it as a sham transaction and without making any additions in the hands of the recipient assessee company, taxed the receipt of shares in the hands of the shareholder of assessee company under section 2(24)(iv) of the Act.

Based on the MOU submitted by the assessee company, Delhi ITAT observed that it was clearly a family arrangement and internal family realignment and therefore, the transfer cannot be termed as gift/ benefit or perquisite. The ITAT also observed that the tax officer cannot hold the transaction as sham by lifting the corporate veil, without providing any cogent reasons, and without appreciating that the beneficiary (i.e. shareholder of assessee company) never obtained any benefit from this transaction at any time. The ITAT thus concluded that the tax officer's observations pertaining to section 2(24)(iv) of the Act were without any jurisdiction and he had overstepped the provisions of the ITA by commenting on the taxability in the hands of a third party assessee (i.e. shareholder of recipient assessee company).

Katalyst comments: *While the ITAT's observation that transfers pursuant to family arrangement cannot be termed as gift/ benefit that could attract taxability will be helpful in analyzing family arrangements in the future, the issue of whether a company can be considered as a party to a family arrangement and can avail benefit of non-taxability of transfers pursuant to family arrangement still remains litigious, considering the existing Bombay HC ruling in the case of B.A. Mohota Textiles[6].*

2. Delhi ITAT holds that non-compete fees should be a non-depreciable capital expenditure[7]

The assessee had acquired the running business of various bottlers. A non-compete fee was paid to the bottlers for not disclosing the confidential information relating to the business and for not competing in similar line of business in their respective territories for a period of 5 years. The assessee followed practice of charging amounts to profit and loss account on a pro-rata basis over 5 years (period of benefit).

The tax officer disallowed the said claim on the basis that it is a capital expenditure. The ITAT observed that the assessee, by virtue of non-compete fee, together with consideration for the purchase of the business, had acquired new business and the said payments were thus for the purpose of acquiring income generating business undertaking. Further, placing reliance on the Delhi High Court's decision in the case of Sharp Business System[8], the ITAT observed that the amount paid as non-compete fees was a capital expenditure that did not qualify for depreciation.

[6] B.A. Mohota Textiles Traders (P.) Ltd. [397 ITR 616 (Bom)]
[7] Hindustan Coca-Cola Beverages Pvt. Ltd [TS-217-ITAT-2020(DEL)]
[8] [2012] 27 taxmann.com 50 (Delhi)

Katalyst comments*: Several judicial precedents (including High Court rulings) on the issue have held that non-compete fees results in a right that is similar in the nature of intangible assets and therefore, eligible to depreciation. Therefore, such a contradicting view by the ITAT merely results in protracted litigation on issues that have already been resolved by higher appellate authorities.*

3. **Gujarat High Court held that loan transaction between sister concerns should not be taxable under section 2(22)(e) of the Act since the shareholder does not receive any 'benefit' from such transaction[9]**

   In the present case, the assessee was a shareholder in a company holding substantial interest (27%) which advanced unsecured loans to its sister concerns, wherein the assessee held substantial interest as well. The issue of taxability of such loan transaction came up at the time of re-assessment and the tax officer contended that since the assessee had substantial interest in both entities, he would have derived a benefit from the said transaction and was therefore, liable to tax under section 2(22)(e) of the Act.

   The High Court observed that there is no provision in section 2(22)(e) of the Act to tax deemed dividends in the hands of the shareholder if the amount has not been received by the assessee shareholder. The High Court further observed that the loan would entail no direct benefit in the hands of the assessee and that mere holding substantial interest in each of the three companies would not render the said sum as deemed dividend under the applicable provisions. Moreover, even though the assessee is a shareholder of the lendee companies, he has not received any sums from the lendee companies. Therefore, in the absence of any benefit having been received by the assessee- petitioner, there was no obligation cast upon him to disclose such transactions and the said sum was not to be taxed as deemed dividend.

   Katalyst comments*: This ruling was in relation to FY 2007-08 i.e. before the amendment that cast the responsibility of paying tax on deemed dividend on the company giving the loan, irrespective of the receipt of such loan by the shareholder. However, after introduction of the Finance Act, 2020, since the dividend liability is shifted to the shareholders, and that DDT has been scrapped, this decision where the High Court has emphasized on the condition that the shareholder should receive a benefit from such loan transaction, would be rendered helpful in the context of inter-company/ group financing.*

[9] Jayesh T Kotak [TS-206-HC-2020(GUJ)]

4. Bombay High Court upheld non applicability of waiver of loan[10]

In yet another case on the long-standing controversy of taxability of waiver of loan, the Bombay High Court held that waiver of loan does not amount to cessation of trading liability and therefore, section 41(1) of the Act should not apply to the said waiver.

In the present case, the tax officer had considered the loan amount waived off by the Government of Maharashtra as income taxable under sections 28(iv) and 41(1) of the Act. On appeal, both, the CIT(A) as well as the ITAT placed reliance on the Bombay High Court ruling in the case of Mahindra and Mahindra[11] and held that the remission of loan would not be chargeable to tax under section 28(iv) as well as section 41(1) of the Act. Upon appeal, the Bombay High Court observed that the case of Mahindra and Mahindra, on which the CIT(A) and ITAT had placed reliance, had been contested by the revenue in the Supreme Court[12] on the same issue. Placing reliance on the ruling of the Supreme Court in the case, the Bombay High Court concluded that the facts of the case are similar to the case considered by the Supreme Court and therefore, the ratio laid down by the Supreme Court should apply to the present case i.e. (i) since the waiver of loan is not in the form of benefit or perquisite other than in the shape of money, it cannot be taxable under section 28(iv) of the Act, and (ii) waiver of loan does not amount to cessation of trading liability and therefore, cannot be taxable under section 41(1) of the Act.

Katalyst comments: *The NPA situation in India has been bad for some years, and Covid-19 will certainly make it worse. The reality is that banks and NBFCs will take haircuts, and in that context, the borrowers will do a corresponding write back. The grave economic situation is such that uncertainty regarding such write back needs to be removed. In the context of the favourable judicial presents anyway, the CBDT should come up with a circular to clarify non-taxability of such write backs.*

5. Supreme Court derecognizes the principle of mutuality; denies exemption on 'surplus' franchisee advertising contributions[13]

The judgement revolves around the doctrine of mutuality which emphasizes on the fact an amount received from oneself cannot be construed as income and hence, not taxable. The Assessee-company was incorporated by Yum Restaurants India Pvt. Ltd ("YRIPL") as its fully owned subsidiary after having obtained the necessary requisite approvals.

The said approvals were sought so as to economize the cost of advertising and promotion for all the francisees of YRIPL as per their needs and were subject to certain conditions as regards

[10] SICOM Limited [116 taxmann.com 410 (Bom)]
[11] Mahindra and Mahindra Ltd [261 ITR 501 (Bom)]
[12] Mahindra and Mahindra Ltd [404 ITR 1 (SC)]
[13] Yum! Restaurants (Marketing) Private Limited [TS-211-SC-2020]

functioning of assessee, whereby it was obligated to operate on a non-profit basis on principles of mutuality.

However, the assessee-company undertook a commercial venture wherein contributions were accepted both from members as well as non-members. Moreover, one member YRIPL was vested with a myriad set of powers to control functioning and interests of other members (franchisees), even to their detriment.

Basis the above, the Apex Court held that such an integration could not be termed as a case of ordinary social association devoid of commerciality. Revenue Authorities were justified in refusing to acknowledge assessee as a mutual concern and denying it any exemption from taxability.

Katalyst comments*: The essence of the principle of mutuality lies in the commonality of the contributors and the participants who are also the beneficiaries. The contributors to the common fund must be entitled to participate in the surplus and the participators in the surplus are contributors to the common fund. This principle thus postulates that no amount of surplus or profit can arise when one undertakes a transaction which oneself. Hence, the Apex Court has denied the benefits that would arise in case the principle of mutuality was applicable to the assessee.*

Corporate Law Highlights

1. Mumbai NCLT approves demerger of investment business from wholly owned subsidiary company into Parent[14]

The said Scheme of Arrangement ("Scheme") was for demerger of investment business from the wholly owned subsidiary i.e. the demerged company by the name of Ensemble Holdings and Finance Limited ("EHFL") to its parent entity or the resulting company being Godrej Industries Limited ("GIL").

The said demerger aimed at achieving the following:
(i) consolidation of investment of EHFL in GIL and (ii) flexibility to GIL to exit from the NBFC activities of EHFL and to transfer shares of EHFL having NBFC License to another promoter group entity at fair value.

Certain key facets of the Scheme that are noteworthy are that the composition of the undertaking being the NBFC license sitting in the subsidiary along with strategic investment being a very nominal stake (0.60% in this case) in the real estate arm being Godrej Properties Limited.

The said scheme facilitates consolidation of investments of EHFL with GIL, while enabling transfer of shares of EHFL (and therefore, the NBFC license) to the promoter group entity.

[14] Godrej Industries Limited [LSI-274-NCLT-2020(MUM)]

Katalyst comments: *For a demerger to be tax neutral, one of the basic conditions is that the demerger should be that of an "undertaking" (i.e. the assets and liabilities so demerged should constitute a business activity). However, in case of demerger of investments, whether such investments, albeit strategic in nature, could constitute an "undertaking" would require further evaluation, basis the facts of each case. Further, even if such demerger is considered as tax neutral, one would need to evaluate whether such investments so demerged could be deemed as "distribution of assets" and therefore, be deemed as dividend u/s 2(22)(a) of the Income-tax Act, 1961.*

C. RBI and Foreign Exchange Regulations Highlights

1. The Ministry of Finance further amends the Foreign Exchange Management (Non-debt Instruments) Rules, 2019[15]

The Ministry of Finance notified the long-awaited Foreign Exchange Management (Non-debt Instruments) (Second Amendment) Rules 2020 giving effect to the following changes:

a. Acquisition through renunciation of rights

Prior to this amendment, any non-resident could have subscribed to renounced shares (i.e., renounced either by a non-resident or a resident) at a price determined by the company (in case of a listed company) or at a price not less than the price offered to residents (in case of an unlisted company).

A non-resident can now subscribe to renounced shares in a rights issue, which have been renounced by a resident in its favor, subject to the pricing guidelines prescribed. This differential pricing shall lead to a separate price in a single rights issue for renounced shares intended to be subscribed by a non-resident, so far as unlisted companies are concerned.

b. Sourcing Norms under Single Brand Retail Trade ("SBRT")

Prior to the amendment, the sourcing norms applicable to SBRT transactions, shall not be applicable up to 3 years from commencement of the business i.e. opening of the first store in cases of products having 'state-of-art' and 'cutting-edge' technology.

SBRT entities are permitted to undertake retail trading through e-commerce. As per the amendment, this exemption of sourcing requirements is now available for up to 3 years from the commencement of business i.e. *opening of the first store or start of online retail, whichever is earlier.*

[15] MINISTRY OF FINANCE (Department of Economic Affairs) NOTIFICATION S.O. 1374(E), April 27, 2020

c. **Sectoral Cap for Insurance Sector and related conditions**

The amendment also notified the government's budget proposal to permit up to 100% FDI in insurance intermediaries under the automatic route, which was earlier capped at 49%.The government has also prescribed certain conditions related to ownership & control of an Indian insurance company by resident Indian entities and operational aspects of insurance intermediaries such as prior IRDAI approval for repatriating dividend, no payments to the foreign group or promoter or subsidiary or interconnected or associate entities beyond the limits prescribed by IRDAI.

Katalyst comments: *While this is certainly a welcome move since the intention of the government to permit 100% FDI under the automatic route for investment in insurance intermediaries is now aligned with specific amendment under the FDI regime, certain other amendments, such as Guidelines on Indian Owned and Controlled" dated 19th October 2015 prescribed by the IRDAI, would also need to be amendment since the said guidelines still require an insurance intermediary to be owned and controlled by Indian investors, which would not be the case if more than 50% ownership is held by foreign investors*

d. **Disinvestment by Foreign Portfolio Investors ("FPIs")**

In case of breach of the prescribed limit for FPIs, they have an option of divesting their excess holdings within 5 trading days from the date of the settlement of trades causing the breach. If the FPI chooses not to divest, then its entire investment in the Indian company is considered as a Foreign Direct Investment ("FDI") and such FPI and its investor group is not permitted to make any further portfolio investments in the Indian company. Such breach is not considered as a contravention of the NDI Rules during the time taken to follow the said procedure. The Amendment has introduced an additional condition i.e., the divestment of holdings by the FPI and the reclassification of FPI investment as FDI will be subject to further conditions, if any, specified by SEBI and the Reserve Bank of India in this regard.

2. The Ministry of Finance Non – Debt Instrument Rules to curb opportunistic takeovers[16].

In order to curb the opportunistic takeovers/acquisitions of Indian companies due to the current COVID-19 pandemic, the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 have been amended to include the following:

- an entity of a country, which shares land border with India or the beneficial owner of an investment into India who is situated in or is a citizen of any such country, shall invest only with the Government approval;

[16] MINISTRY OF FINANCE (Department of Economic Affairs) NOTIFICATION S.O. 1278(E), April 22, 2020

- A citizen of Pakistan or an entity incorporated in Pakistan shall invest only under the Government route, in sectors or activities other than defence, space, atomic energy and such other sectors or activities prohibited for foreign investment;
- In the event of the transfer of ownership of any existing or future FDI in an entity in India, directly or indirectly, resulting in the beneficial ownership falling within the restriction or purview of the above restrictions, such subsequent change in beneficial ownership shall also require government approval.

Katalyst comments: *The earlier FDI policy provided country specific restrictions only with respect to Pakistan and Bangladesh. The scope of restrictions has now been extended as described above. Various statistical surveys suggest that, various start-ups in India are funded by Chinese funds and the above-mentioned restriction would only further dent the capital-deficiency in the country. Also, while Hong Kong is a part of China, it has been classified as a separate country by the Indian Government for FDI reporting purposes. To avoid unintended impact on FDI inflows from Hong Kong, the Ministry should issue an appropriate clarification on the matter.*

3. RBI issues Governors' Statement[17] in response to the Covid 19 Crisis

Basis the continuing assessment of the macro economic situation and financial market conditions, the RBI proposes to take the measures in the following areas being:

i. Maintaining adequate liquidity;
ii. Facilitate and incentivise bank credit flows;
iii. Ease finanacial stress;
iv. Enable the normal functioning of markets

The table below captures the detailed insights of the various measures suggested in the Governors' Statement. These have been broadly categorized into two broad baskets i.e. liquidity management and regulatory measures. Some key measures have been elaborated in the table below:

Sr. No.	Suggested Measures	Implications
Liquidity Management		
1.	Targeted Long Term Operations (TLTRO) 2.0	It has been decided to conduct targeted long-term repo operations (TLTRO 2.0) for an aggregate amount of INR 50,000 crore, to begin with, in tranches of appropriate sizes.
2.	Refinancing Facilities for All India Financial Institutions (AIFIs)	In the wake of the ongoing pandemic, it has been decided to provide special refinance facilities for a total amount of INR 50,000 Crores to various financial institutions such as NABARD, SIDBI and NHB to facilitate them to meet sectoral credits.

[17] Governors' Statement dt. April 17, 2020

3.	Liquidity Adjustment Facility: Fixed Rate Reverse Repo Rate	In order to deploy the excess liquidity with the commercial banks towards more productive sectors in the economy; it has been decided to reduce the fixed rate reverse repo rate under the liquidity adjustment facility (LAF) by 25 basis points from 4.0 % to 3.75 %
Regulatory Measures		
4.	Asset Classification	• The Asset Classification norms have been put to a standstill in the moratorium period from March 1, 2020 to May 31, 2020. • Insofar as the risk built up in the bank balance sheets is concerned, a higher provision of 10 % on all such accounts under the standstill, spread over two quarters, i.e., March, 2020 and June, 2020 is suggested. These provisions can be adjusted later on against the provisioning requirements for actual slippages in such accounts.
5.	Extention of Resolution Timeline	In the case of large accounts under default, Scheduled Commercial Banks, AIFIs, NBFC-ND-SIs and NBFC-D are currently required to hold an additional provision of 20 per cent if a resolution plan has not been implemented within 210 days from the date of such default. This has been further extended by 90 days.
6.	NBFC Loans to Commercial Real Estate Projects	In respect of loans to commercial real estate projects delayed for reasons beyond the control of promoters can be extended by an additional one year, over and above the one-year extension permitted in normal course, without treating the same as restructuring. It has now been decided to extend a similar treatment to loans given by NBFCs to commercial real estate. This will provide relief to NBFCs as well as the real estate sector.

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

1. SEBI provides for certain relaxations to Issue of Capital and Disclosure Requirements ("ICDR") Regulations, 2018 in respect of Rights Issue in the backdrop of Covid 19[18]

In their bid to facilitate fund raising from capital markets in the backdrop of Covid-19, the SEBI has relaxed norms applicable to listed entities for raising funds. These are broadly categorized into three baskets which have been discussed below:

[18] Press Release No 23/2020 dt. April 21, 2020

Rights Issue:

Fast Track Issuances:

- The eligibility requirement for average market capitalization of public shareholding of INR 250 Crs has been reduced INR 100 Crs.
- The requirement relating to period of listing of equity shares for at least 3 years has been reduced to listing for 18 months only.
- The conditions related to no audit qualifications for issuers' audited accounts has been replaced with the requirement to disclose the impact on audit qualifications on issuers financials.

Minimum Subscription:

- The threshold for a minimum subscription requirement has been reduced from 90% to 75% of the offer size subject to certain conditions.

Threshold for not filing Draft Letter of Offer with SEBI:

- The threshold for not filing a Draft Letter of Offer has been increased from INR 10 Crores to INR 25 Crores.

It may be noted that these relaxations are applicable to rights issues that open on or before March 31, 2021.

Further, the SEBI *vide* another circular[19],brought about certain other relaxations which are as follows:

Flexibility on Issue Size:

- If an Offer Document of an issuer is pending approval from SEBI, the issuer shall be permitted to reduce or increase the offer size by 50% of the estimated issue size (in lieu of the present limit of 20%) without filing a fresh offer document.
- This shall be applicable to all documents pending approval up to December 31, 2020 with respect to IPOs/FPOs/Rights issue.

Validity of SEBI Observations:

- The validity of observations on all public issues/rights issues to be extended by 6 months from the date of expiry for issuers whose observation has expired/shall expire between March 1, 2020 and September 30, 2020.

[19] SEBI/HO/CFD/DIL1/CIR/P/2020/66 dt. April 21, 2020

2. **SEBI temporarily relaxes the cooling off period before a fresh issue subsequent to a buy-back[20]**

   Considering the developments relating to the COVID-19 pandemic, and in order to facilitate the grappling demands of funds by the corporates, SEBI has temporarily relaxed the restriction on companies that do not permit them to raise further capital for a period of one year from the expiry of a buyback, except in discharge of their subsisting obligations. The period of one year has now been reduced to 6 months.

3. **SEBI relaxes actions against non-compliance with minimum public shareholding ("MPS") requirement during the period March 1, 2020 to August 31, 2020[21]**

   SEBI circular No. CFD/CMD/CIR/P/2017/115 dated October 10, 2017 lays down the procedure to be followed by the recognized stock exchanges / depositories with respect to MPS non-compliance. However, considering prevailing business and market conditions, the stipulations of the aforesaid October 10, 2017 SEBI circular are relaxed for listed entities for whom the deadline to comply with MPS requirements falls between the period from March 1, 2020 to August 31, 2020. SEBI has also advised the Stock Exchanges to not take any penal action as envisaged in the said circular against such entities in case of non-compliance during the said period (any action initiated after March 1, 2020 may be withdrawn).

E. Others Regulatory Highlights:

1. **NCLAT: CCI order imposing penalty on gun jumping set aside[22]**

   The given decision revolves around the applicability of the *De Minimis Exemption* which would not apply if the sales and assets of an entity would fall below a certain given threshold.

   The facts are Eli- a company based in the United States agreed to acquire the global animal health business of Novartis AG. With respect to the Indian leg of the transaction, the parties believed it to be covered under the then applicable *de Minimis Exemption* which applied to acquisitions of enterprises whose sales in India were not more than INR 750 Crs or whose Indian assets valued not more than INR 250 Crs and hence the Competition Commission of India ("CCI") was not notified.

   However, the CCI, issued a letter asking as to why the transaction was not notified to which Eli responded that the transaction was exempt under the *de Minimis Exemption* as the target

[20] SEBI Circular No. SEBI/HO/CFD/DCR2/CIR/P/2020/69 dt. April 23, 2020
[21] SEBI/HO/CFD/CMD1/CIR/P/2020/81 dt. May 14,2020
[22] NCLAT New Delhi - TA (AT) (Competition) No. 03 of 2017 dt. March 12, 2020

business only had a turnover of INR 93 Crs and assets worth INR 36.2 Crs. However, the parties also decided voluntarily to notify the transaction to CCI.

The CCI further concluded, without citing any reasons, that the transaction was reportable. Although the CCI approved the transaction, it issued a show cause notice to Eli to show cause why it should not be penalized for not notifying the transaction in India. Eli again responded that the transaction was exempt under the *de Minimis Exemption*. Post which, the CCI imposed a penalty of INR 1 Crore by asserting that the thresholds of the *de Minimis Exemption* did not apply to the business being acquired i.e. the Animal Health Business but rather to the target's parent i.e. Novartis India Ltd, which was not covered by the *de mimimis* exemption. This decision was based solely on the ground that the parent was an incorporated entity that animal health business was a mere portion of the entire Indian operations of Novartis.

Aggrieved by the decision of the CCI, Eli approached the NCLAT in appeal contending that such an interpretation of the *de Minimis Exemption* by the CCI was wrong and it had incorrectly applied the thresholds to the target's parent company merely because the target was not incorporated.

The NCLAT also clarified that for the purpose of calculation of assets and turnover what is being acquired is relevant, as the assets/turnover of what is left over with the sellers after the acquisition will have no role to play in the context of the business conducted by the purchaser post acquisition. Accordingly, the NCLAT held that since the turnover and assets attributable to the target was INR 93.9 Crores and INR 36.2 Crores respectively, the transaction was exempt under the *de Minimis exemption* and therefore was not required to be notified to the CCI.

F. Goods and Services Tax (GST)

1. The Delhi High Court[23] declared the time limit of 3 years (till June 30, 2020) for filing GST-TRAN-1 return

The Division Bench of the Hon’ble Delhi High Court (‘’HC’’)has read down Rule 117 of the CGST Rules 2017 (‘’CGST Rules’’), which provide for a time limit in availing transitional credits & held that the time limit prescribed is procedural and directory in nature and that the "CENVAT credit” which stood accrued and vested is a property of the assessee, and is a constitutional right under Article 300A of the Constitution. Further, the HC also held that the benefit of the exception created under Rule 117(1A) of the CGST Rules which allows taxpayers to file Form GST TRAN-01 (‘TRAN-1) belatedly on account of ‘technical glitches’ would equally apply to taxpayers who did not file TRAN-1 in time due to their own follies. Also, the HC adopted the time limit of 3 years from implementation of GST as provided under the Limitation Act, 1963 for filing of TRAN-1 return.

[23] In the matter of Brand Equity Treaties Ltd. & Ors. [TS-256-2020-(DEL)-NT]

Katalyst comments: *Vide this judgment, the Delhi High Court has clearly held that time limit for filing TRAN-1 return prescribed under Rule 117 of CGST Rule is directory and not mandatory. Further, the benefit is not just qua the petitioner, but it is extended to thousands of taxpayers who missed the deadline due to non-technical difficulty. It is also pertinent to note that the Delhi HC has considered a period of 3 years as per Limitation Act for transition of credit to GST regime.*

2. Delhi High Court[24] grants relief by quashing restriction on rectification of 'same period' return imposed by circular 26/26/2017-GST dt. December 29, 2017

The Delhi High Court ("HC") allows the writ filed by the petitioner and reads down para 4 of Circular No. 26/26/2017-GST dated December 29, 2017 to the extent it restricts the rectification of Form GSTR-3B in respect of the period in which the error has occurred. Further, the HC clarified that "petitioner has a substantive right to rectify/adjust the ITC for the period to which it relates" and "the rectification/ adjustment mechanism for the months subsequent to when the errors are noticed is contrary to the scheme of the Act". The HC also held that since the respondents could not operationalise the statutory forms (GSTR-2 & 3) envisaged under the GST Law resulting in depriving the petitioner to accurately reconcile its input tax credit, the respondent cannot today deprive the petitioner of the benefits that would have accrued in favour of the petitioner if, such forms (GSTR-2& 3) would have been enforced. Hence, Petitioners cannot be denied the benefit due to the fault of the respondents. The HC allowed petitioner to rectify GSTR-3B for the period July 2017 to September 2017 to which the error relates.

Katalyst comments: *Allowing the rectification of GST returns for the period to which the error relates is a welcome move. There is no provision under the GST law which restricts rectification of return for the period to which error relates and any circular restricting such rectification should be in conformity with the GST Law. However, GST authority should suitably amend the GST Law to avoid any future ambiguity.*

3. Kerala High Court[25] directs release of goods as difference in address as per invoice and as per E-way bill is a clerical mistake

The Kerala High Court has held that difference in address as per invoice and as per E-way bill is a clerical mistake and not a serious mistake as the petitioner has complied with all the provisions of the CGST Act and hence, revenue should justify detention and penalty proceedings. Further, the High Court also directed to release the goods detained on furnishing of bank guarantee.

[24] In the matter of Bharti Airtel Ltd. Vs. UOI [TS-257-HC-2020-(DEL)-NT]

[25] In the matter of M.R. Traders Vs. Assistant State Tax Officer, State GST Department [TS-262-HC-2020(KER)-NT]

4. **Notifications granting relief in view of Covid-19**

- **Extension in time-limit of Annual return and reconciliation statement[26]–** Due date of filing of Form-GSTR-9(Annual return) and Form GSTR-9C (reconciliation statement) for F.Y. 2018-19 has been extended from June 30, 2020 to September 30, 2020.

- **Extension of validity of E-way bills[27] –** The due date of E-way bill generated on or before March 24, 2020 and having date of expiry between March 20, 2020 to April 15, 2020, has been extended to May 31, 2020

- **Amendment in special procedure for corporate debtors undergoing the corporate insolvency resolution process under the IBC, 2016[28]**

  - Corporate debtors who have filed Form GSTR -1 and Form GSTR -3B for all the tax periods prior to the appointment of interim resolution professionals (IRP) or resolution professionals (RP) are not required to obtain a separate registration with effect from the date of appointment of IRP/RP.

Corporate debtors can obtain registration within 30 days of the appointment of IRP/RP or by June 30, 2020, whichever is later.

Do feel free to reach out to us for a detailed discussion on ketan.dalal@katalystadvisors.in

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[26] Notification no. 41/2020-CT dated May 5, 2020
[27] Notification no. 40/2020-CT dated May 5, 2020
[28] Notification no 39/2020-CT dated May 5, 2020