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Katalyst Kaleidoscope

November 2024: Tax and Regulatory Insights

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A. Income Tax Highlights

1. Delhi HC: Invokes 'notional' income theory in context of quantum of ESOP taxation[1]

In the present case, the assessee, under an Employee Stock Purchase Scheme (ESPS) was allotted 11,50,500 shares at ₹15 per share, which had a market rate of ₹49.45. The shares were subject to a lock-in period: 25% were restricted for 12 months, and the remaining 75% for 18 months, rendering them **non-transferable** within that period.

During assessment, the AO determined that the difference of INR 34.45 per share between the concessional rate of INR 15 and the market price of INR 49.45 was taxable as a perquisite under Section 17(2)(iiia) of the IT Act. The matter went before the Delhi High Court wherein it was held that in light of the restriction with respect to marketability and tradability of the stock in question, the FMV could not exceed the face value of the shares, i.e., ₹15 per share, and further emphasized that shares under restriction do not accrue any real taxable income and reaffirmed that it is a well-established principle of Indian tax law that notional income is not taxable. Consequently, the FMV was to be taken as ₹15 per share, for determining the quantum of taxable income; negating any additional tax liability based on the market value.

Katalyst comment:

The judgment reinforces the principle that shares with restriction of transfer cannot be compared to fully tradable shares in terms of market value; the presence of significant encumbrances and restrictions on an asset's tradability means that it should not be valued at its unrestricted market value, as the taxpayer cannot freely realize that value.

2. ITAT Rajkot: Deemed Gift Concept u/s 56 not attracted to shares received under amalgamation; also not regarded as a transfer u/s 47(ii)[2]

In the present case, assessee received shares on an amalgamation of companies; the case was re-opened by the Assessing Officer on the contention that the shares received on amalgamation were received at a consideration exceeding fair market value, resulting in an undisclosed income of ₹1.97 crore and added the same to the assessee's total income u/s 56(2)(vii)(c)(ii) of the Act (which taxes property received without consideration or inadequate consideration).

The assessee argued that Section 56(2)(vii)(c)(ii) does not override Section 47(vii) of the IT Act and as per Section 47(vii) shares received on an amalgamation or demerger are not considered "transfers" and accordingly are not subject to capital gains tax. The assessee further contended that clause (h) of second proviso to section 56(2)(vii)(c)(ii) specifically excludes/exempts such transactions.

[1] Ravi Kumar Sinha [TS-590-HC-2024(DEL)] dated August 14, 2024
[2] Kruti Rajesh Doshi [TS-796-ITAT-2024(Rjt)] dated October 28, 2024

The matter went before the ITAT wherein ITAT upheld the CIT(A)'s decision and held that the **shares received on amalgamation does not constitute a "transfer" under Section 47(vii) and since there was no transfer, the shares were received under a court-approved amalgamation cannot be subject to tax.**

Katalyst comment:

This case is an example of how such totally unwarranted and unnecessary litigation can burden taxpayers and the judicial system, especially when settled law clearly provides that shares received on amalgamation are not considered "transfers" under Section 47(vii); the ITAT's decision underscores the need for avoiding such litigations that consumes judicial resources and taxpayer time without any justifiable grounds.

3. ITAT Mumbai: Assessee eligible for selection of more beneficial provision; allows carry forward of STCL[3]

In the present case, Assessee, a tax resident of Mauritius while filing return of income claimed an exemption of long-term capital gains (LTCG) of Rs. 68 Lacs under Article 13(4) of the India-Mauritius Double Tax Avoidance Agreement (DTAA) and declared brought forward short-term capital losses (STCL) of Rs. 885 Cr for carry forward. During the assessment proceedings, the Revenue, denied the carry forward of these losses, arguing that the Assessee could not selectively apply DTAA benefits and the Income Tax Act provisions.

On appeal, ITAT held in favor of the assessee, allowing it to choose the more beneficial provisions of either the Income Tax Act, 1961, or the India-Mauritius DTAA as per Section 90(2) and accordingly the Assessee could apply the DTAA's beneficial provisions for exempting LTCG under Article 13(4) while using domestic law provisions to carry forward STCL without setting them off against the LTCG. Placing reliance on judicial precedents of *J.P. Morgan India Pvt. Ltd.*, *Credit Suisse (Singapore) Co. (Mauritius)*, and *Indium IV (Mauritius) Holding*, ITAT affirmed that an assessee can selectively apply DTAA provisions where beneficial, for distinct streams of income.

Katalyst comment:

The ITAT's ruling reaffirms the principle of providing the assessee with the benefit of selecting the more beneficial provisions provided under DTAA and Income Tax regulations, and thereby ability to optimize the tax positions for distinct streams of income.

[3]Morgan Stanley Mauritius Company Ltd [TS-807-ITAT-2024(Mum)] dated November 05, 2024

4. CBDT: Fixes monetary limits for reduction or waiver if interest u/s 220(2) of the Income Tax Act[4]

By virtue of powers specified u/s 220(2A) of the IT Act vested with the income tax authorities, CBDT has provided for the following monetary limits empowering the respective income tax authorities to reduce or waive the interest payable u/s 220(2) of the IT Act (which provides for payment of interest @1% p.m or part thereof for failure to make payment of demand specified u/s 156):

Sr No	Income Tax Authority	Monetary Limits for reduction or waiver of interest
1	Pr. CIT/CIT	Upto Rs. 50 lacs
2	CCIT/DGIT	Above Rs. 50 lacs to Rs. 1.5 crore
3	Pr. CCIT	Above Rs. 1.5 crore

The reduction or waiver of interest shall be subject to satisfaction of all the following conditions:

- payment of such amount has caused or would cause genuine hardship to the assessee;
- default in interest payment was due to circumstances beyond the control of the assessee; and
- the assessee has cooperated in inquiry relating to assessment or proceeding of the recovery of any amount due from him

B. Corporate Law Highlights

1. Supreme Court (SC): Settles the law on 'Certified copies' for filing appeal against NCLT Orders[5]

In the case of State Bank of India vs. India Power Corporation Ltd., the Supreme Court addressed whether a "free of cost" certified copy qualifies as a "certified copy" for filing appeals before the NCLAT. Rule 50 of the NCLT Rules mandates the Registry to provide a certified copy of final order passed to the parties concerned free of cost, whereas Rule 22(2) of the NCLAT Rules mandates appeals be filed with a certified copy, leading to ambiguity over whether a free copy satisfies this requirement.

The Supreme Court held that both "free of cost" and "paid" certified copies are valid for appeals under Rule 22(2) of the NCLAT Rules. However, litigants must demonstrate diligence by applying for a certified copy upon pronouncement of the order, as waiting indefinitely for a free copy is not permitted. The Court condoned SBI's delay in filing the appeal as the same was within the condonable period and aaffirmed that under Rule 50 of the NCLT Rules, free and paid certified copies are equivalent for the purpose of filing appeals.

[4] CBDT Circular No 15/2024 dated November 04, 2024

[5] *State Bank of India v. India Power Corporation Ltd.*, Civil Appeal 10424 of 2024

2. **NCLT Bengaluru: Compliance with Section 66, unanimous shareholder approval and no creditor objections- warranted admission of capital reduction.[6]**

In the matter of *Wipro Enterprises Pvt. Ltd.* ("the Company"), the NCLT Bengaluru Bench approved a petition under Section 66 of the Companies Act, 2013, permitting the reduction of the Company's paid-up share capital. This approval was granted on the basis that the reduction had been unanimously approved by shareholders through a special resolution, no creditors had raised objections, and the Company had fulfilled all statutory requirements under Section 66 related to share capital reduction.

A creditor, *Zenith Metaplast Pvt. Ltd.*, with whom the Company had an ongoing arbitration before a sole arbitrator in Mumbai, objected before the NCLT, claiming its outstanding dues. The Company countered that Zenith's claims were false and that any legitimate claims would be addressed within the arbitration proceedings, not in the NCLT. Additionally, the Company emphasized its financial stability and noted that no other creditors, representing over 99.9% of the Company's total debt value, had raised objections to the capital reduction, nor had Zenith questioned the Company's financial standing.

The NCLT observed that Zenith's claims were under arbitration and that its interests would not be adversely impacted by the proposed capital reduction. The tribunal admitted the petition given the unanimous shareholder's approval and the Company's full compliance with Section 66 requirements.

3. **NCLT Mumbai: directed purchase of shares held by the minority shareholder to resolve internal disputes[7]**

In the present case, Mr. Jackie Shroff (the Petitioner), a minority shareholder of Atlas Equifin Pvt. Ltd ("the Company"), filed a petition before the NCLT, Mumbai Bench, alleging oppression and mismanagement by the majority shareholders of the Company and requested that the Company be directed to buy his shares; the key allegations included:

- failure to hold AGMs on time;
- non-distribution of substantial profits as dividends;
- misuse of company funds;
- refusal to provide access to statutory records; and
- failure to return share application money.

[6] Wipro Enterprises (P.) Ltd [2024] 165 taxmann.com 700 (NCLT-Beng.) dated July 20, 2024

[7] In the matter of Jackie Shroff vs Atlas Equifin (P.) Ltd [2024] 167 taxmann.com 722 (NCLT - Mum.) dated February 10, 2023

Relying upon the judgment in the case of M.S.D.C. Radharamanan v. M.S.D.Chandrasekara Raja & Anr. (2008) 6 SCC 750, the Counsel for the Petitioner submitted that the powers of the Tribunal in a matter under Sections 397 and 398 of the Companies Act, 1956 (equivalent to Sections 241 and 242 of the Companies Act, 2013), are very wide and the Tribunal has the power to grant relief even if a case of oppression and mismanagement is not made out and the Tribunal can direct the purchase of shares of the Petitioner by another member of the Company under the provisions of Section 242(2) of the Companies Act, 2013.

The NCLT observed that to resolve disputes and ensure the Company's smooth operation, it would be equitable to have Petitioner's shares bought by the Company. Accordingly, the tribunal appointed a Chartered Accountant to determine the fair market value of the shares for this transaction and ordered the company to purchase Shroff's shares under Section 242(2)(b) of the Companies Act, 2013.

C. SEBI and Other Highlights

1. SEBI: Master circular for complying with LODR Regulations, 2015 by listed entities [8]

SEBI has issued a master circular for compliance with the provisions of SEBI LODR Regulations, 2015 (LODR Regulations) by listed entities; the circular updates and supersedes the Master Circular dated July 11, 2023, by incorporating all relevant circulars issued up to September 30, 2024.

The Master Circular provides a chapter-wise framework for compliance with various obligations under the LODR Regulations addressing periodic disclosures, financial disclosures, annual disclosures, event based disclosures, corporate governance, and other obligations.

2. SEBI: Proposes review of definition of Unpublished Price Sensitive Information (UPSI) under SEBI (Prohibition of Insider Trading) Regulations, 2015[9]

SEBI has issued a consultation paper proposing review of the definition of Unpublished Price Sensitive Information under SEBI (PIT), 2015 to bring regulatory clarity, certainty and uniformity of compliance in the ecosystem. The key proposals are summarized below:

- **Disclosure of Agreements**: Companies must disclose any agreements that could impact management and control to ensure transparency of corporate structure changes.

[8] Notification No SEBI/HO/CFD/PoD2/CIR/P/0155 dated November 11, 2024
[9] SEBI Consultation Paper issued on November 09,2024

- **Managerial Changes**: Disclosure of changes in key personnel that could impact the leadership and decision-making of the company and any enforcement actions against them that could affect the company's reputation or operations.

- **Fraud and Defaults**: Immediate disclosure of any fraud or defaults by the company or its key personnel.

- **Arrest of Key Personnel**: Any arrest of top managers must be disclosed to maintain investor confidence and market perception.

- **Capital Structure Changes**: Such as new share issuances or major changes in ownership must be disclosed to stock exchanges within 30 minutes post board approval.

- **Other Corporate Developments**:

    - **Loan Settlements**: Disclosure of loan restructuring or settlements.
    - **Insolvency**: Prompt updates on insolvency proceedings or outcomes.
    - **Legal Disputes**: Major disputes or litigation outcomes having significant financial impact must be disclosed.
    - **Licensing**: Updates on essential licenses or regulatory approvals must be disclosed.

3. SEBI: Standard Operating Procedures under SEBI (Prohibition of Insider Trading) Regulations 2015[10]

The BSE and NSE circulars have mandated unlisted companies, which are getting listed pursuant to any scheme as approved by NCLT, to submit Structured Digital Database Certificate from Practicing Company Secretary (PCS) at the time of filing of application with the Exchanges, certifying that the Company is compliant with Regulation 3(5) and 3(6) of SEBI (PIT) Regulations, 2015 and any amendment thereof (which provides for internal control mechanism for preservation of Unpublished Price Sensitive Information (UPSI)).

Regulation 3(5) mandates maintaining a tamper-proof digital database that records the nature of UPSI, details of individuals sharing/receiving it, with controls like time-stamping and audit trails and ensuring same is not outsourced**.** Regulation 3(6) provides for preserving the structured digital database for at least eight years or until the completion of any investigation or enforcement proceedings, if applicable**.**

[10] BSE Notice No -20241113-13 and NSE Notification. No: NSE/CML/2024/35 dated November 13, 2024

4. SEBI: Analysis of Royalty Payments by Listed Entities to Related Parties (RPs) RBI[11]

SEBI has issued a paper which has captured its analysis of royalty payments made by listed entities to related parties and the paper has identified following key areas of concerns for the regulator's:

- Lack of transparency for royalty payments;
- inconsistent disclosures on purpose, rationale, royalty rates and benefit arising to shareholders;
- Royalty payments made despite limited or no correlation with performance;
- Some payments are termed differently (e.g., management fees, Technology License fees etc) to bypass regulatory thresholds;
- Royalty payments are higher compared to dividend payment made;
- Royalty payments by loss making companies; and
- Significant payments towards brand usage, despite the royalty-paying companies themselves spending significantly on advertisement & brand promotion

Katalyst comment:

It is anticipated that SEBI may come up with stricter regulations in the context of adequacy of payments and disclosure requirements including review of policies for determining materiality of royalty payments to RPs, thresholds based on profitability, scrutiny of companies paying royalty while incurring losses, sunset provisions to prevent indefinite payments, etc.

5. SEBI: Exonerates Piramal Pharma for alleged LODR violations due to absence of "materiality criteria" impacting market perception[12]

SEBI investigated Piramal Enterprises Limited (PEL) for allegedly failing to disclose material information concerning two key events:

- penalty of ₹8.32 crore imposed by the National Green Tribunal (NGT) in 2019 for water pollution by PEL's pharmaceutical unit; and
- shutdown of a PEL plant in 2018 ordered by the Telangana State Pollution Control Board (TSPCB) due to pollution concerns

In 2020, the pharmaceutical business of PEL, including liabilities, was transferred to Piramal Pharma Limited (PPL), a subsidiary of PEL which was subsequently listed on stock exchanges in October 2022. SEBI alleged that PEL's failure to disclose the aforesaid events violated SEBI's Listing

[11] SEBI Research Paper dated November 14, 2024
[12][LSI-1144-SEBI-2024-(MUM)] dated November 11, 2024

Obligations and Disclosure Requirements (LODR) Regulations and that PPL as the successor to PEL's pharmaceutical unit, was responsible for these disclosure lapses under the terms of a demerger arrangement.

Though the adjudicating officer exonerated PPL, SEBI had issued a new Show Cause Notice (SCN), intending to impose penalties and upon further review:

- SEBI upheld the adjudicating officer's exoneration as the responsibility to disclose the material events if any, rested with PEL not PPL since PEL was neither listed nor in existence when the aforesaid events occurred;

- The events under question did not meet the criteria of "materiality" set by SEBI's LODR Regulations, which mandate that only information likely to significantly impact market perception requires disclosure and the penalty and plant shutdown were deemed immaterial based on revenue and impact analyses, as well as confirmations from the National Stock Exchange (NSE).

- SEBI noted that while the penalty and plant shutdown were included in PPL's 2023 Business Responsibility Report, the events did not generate any significant market response that warranted a prior disclosure.

6. RBI: Directs exercise of due diligence by Authorized dealers in case of cross border corporate guarantees[13]

Having encountered the instances of guarantees (such as Standby Letters of Credit (SBLCs) or performance guarantees) issued by persons resident outside India in favor of Indian residents, which are not in compliance with the existing FEMA regulations, RBI has advised that such guarantee contracts must be in accordance with concerned FEMA Regulations.

To ensure adherence to FEMA regulations, RBI has directed Authorized Dealer (AD) Category-I banks to verify that all guarantee contracts they advise to or on behalf of their resident clients align with FEMA guidelines and additionally banks are encouraged to inform their clients of this regulatory requirement.

7. ICSI: Governance and Compliance Standard on PoSH Act[14]

The Institute of Company Secretaries of India (ICSI) has issued the Governance and Compliance Standard for the Prevention of Sexual Harassment (PoSH) Act, which shall be applicable to all workplaces, whether in the public or private sector irrespective of their size and nature of business, area of operations, etc. Key elements of the standard include:

[13] RBI Circular No RBI/2024-25/79 dated October 04, 2024
[14] Governance and Compliance Standard on POSH Act, September, 2024

- **Policy and Training Requirements**: The Employer whether public, private or not-for-profit organization having 10 or more Employees, to formulate a Policy PoSH Act or may authorize the Internal Committee (IC) to formulate the Policy. The policy shall be communicated to all stakeholders (every office / administrative unit of the Workplace). Regular training and sensitization programs are recommended for all employees, including specific training for IC members to ensure effective handling of complaints.

- **Internal Committee Formation and Roles**: Organizations with 10 or more employees must establish an Internal Committee (IC) to handle complaints related to sexual harassment. The Presiding Officer (chairperson of the Internal Committee nominated by the Employer who shall be a woman employed at a senior level) will convene at least 2 review meetings each year to assess the effectiveness of the policies.

- **Complaint and Inquiry Mechanisms**: Clear procedures to be outlined for filing of complaints, inquiry process, confidentiality requirements, and timelines for resolving cases, emphasizing non-retaliation for complainants and witnesses.

- **Annual Reporting and Gender Equality**: The document requires annual reporting of sexual harassment cases and recommends a gender-neutral approach to foster a safe and inclusive work environment for all.

D. Goods and Service Tax Highlights

1. Supreme Court (SC)[15] : reviews its earlier judgement and holds that Directorate of Revenue Intelligence (DRI) is empowered to issue SCN demanding customs duty

The SC, in 2021, relying on its earlier judgment[16]**,** in the matter of the taxpayer[17], had ruled that an officer of the DRI is not a 'proper officer' in terms of section 2(34) of the Customs Act, 1962**.**

Later, a review petition was filed by the Department of Revenue and was pending; meanwhile, the ratio of the said judgement was followed by the various High Courts and High Courts have quashed the SCNs issued by the DRI. Now, based on examination of the provisions, submissions, past rulings, etc, the SC has held that DRI officers are officers of Customs and are proper officers who can issue SCNs under section 28 of the Customs Act.

[15] Commissioner of Customs vs. M/s Canon India Pvt. Ltd. [2024-TIOL-115-SC-CUS-LB] dated November 7, 2024
[16] Commissioner of Customs *v.* Sayed Ali [2011] (265) ELT 17 (SC)
[17] CC vs. M/s Cannon India Pvt. Ltd. [2021-TIOL-123-SC-CUS-LB] dated March 9, 2021

Katalyst comment:

It is pertinent to note that under the GST, a notification[18] has been issued appointing the Directorate General of Goods and Services Tax Intelligence (DGGI) officers as 'Central tax officers' under the CGST Act and empowering them with all the powers under CGST Act and the IGST Act. Also, it should be kept in mind that though similar, GST provisions in this regard are not in pari materia with the Customs Act; therefore, the SC review order may not directly extend to GST law.

2. Kerala (HC) – Rule 96(10) of the CGST Rules held as 'unconstitutional' as it ultra vires section 16 of the IGST Act and violates the constitutional provisions[19]

The Kerala HC has held that working of Rule 96(10) of the CGST Rules has resulted in hostile discrimination amongst exporters who opt to apply for a refund under section 16(3)(a) and section 16(3)(b) IGST Act and such discrimination is not contemplated by Section 16 of the IGST Act, on the right to refund. Hence, rule 96(10) of the CGST Rules is ultra vires to section 16 of the IGST Act and violates constitutional provisions.

The court further directed that any action which has been already initiated by way of a show cause notice or culminated in an order against the petitioners based on rule 96(10) of the CGST Rules will stand quashed and no proceedings shall be taken to recover any IGST that has been refunded to petitioners for the period between October 23, 2017, and October 8, 2024.

In addition to the above, the court observed that Rule 96(10) of the CGST Rules was deleted vide Notification no. 20/2024 – CT, dated October 8, 2024; however, this was done on a prospective basis. Hence, the amendment does not deal with scenarios where refund was denied in the period when the sub-rule was active.

***Katalyst comment**:*

The High Court's decision that no recovery should be made for refund allowed during the period October 23, 2017, and October 8, 2024, holding that the rule is 'unconstitutional', is a welcome move.

[18] Notification No.14/2017–Central Tax dated July 1, 2017
[19] Vinayaka Cashew Company Vs. UOI dated [2024-TIOL-1859-HC-KERALA-GST] dated October 10, 2024