

## Katalyst Kaleidoscope

October 2022: Tax and Regulatory Insights

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### A. Income tax highlights

#### 1. **Supreme Court<sup>1</sup>: Locked in listed shares not considered as ‘quoted shares’ for valuation**

The Supreme Court recently held that for the purpose of valuation under erstwhile Gift Tax Act, shares locked in as per the SEBI Regulations shall not be considered as ‘quoted shares’ since such shares are barred by SEBI from being freely transferable. Further, the ability to transfer such shares inter-se between the promoters during the lock-in period would not render the locked-in shares as ‘quoted shares’ because it is not possible to get the quotation of inter-se transfer in the ordinary course of business.

***Katalyst Comments:***

*The aforementioned principles should also be applicable to deemed income provisions under the deemed gift provisions under Section 56(2)(x) of the Income-tax Act, 1961 (“Act”) on receipt of quoted-but-locked-in shares inter-se between promoters at a price lower than the current market price.*

#### 2. **Supreme Court<sup>2</sup>: Delayed deposit of employees; contribution to PF/ESI disallowed**

The Supreme Court held that the delayed deposit of employees’ contribution by the employer beyond the due date as mentioned in the respective Acts (i.e., PF/ ESI) shall not be allowed as a deduction, even if it is paid before the due date of filing return of income.

***Katalyst Comments:***

*The aforesaid decision is in line with the amendment made in Finance Act, 2021 in relation to deposit of employees’ contribution to PF/ ESI by the employer u/s 36(1)(va) of the Act.*

#### 3. **Supreme Court<sup>3</sup>: Charitable institution carrying on object of General Public Utility – implications of carrying on activity for profit**

The Supreme Court combined various appeals in the context of myriad charitable institutions ranging from ICAI, cricket associations, statutory authorities (such as Ahmedabad Urban Developing Authority) notified under Section 10(46), trade promotion bodies, non-statutory bodies like ERNET, NIXI, GS1 India and trusts. The context was that there is an exemption (subject to certain conditionalities), in relation to institutions carrying out charitable activities, which is defined as including, inter alia, relief of the poor, education and ‘the advancement of any other object of General Public Utility (‘GPU’). There is a proviso to Section 2(15)(1) which disentitles the last limb from tax exemption unless such activity is undertaken in the course of

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<sup>1</sup> DCIT v BPL Ltd (SC) (Civil Appeal No. 3265 of 2016)

<sup>2</sup> Checkmate Services Pvt Ltd v CIT (SC) (Civil Appeal No. 2833 of 2016)

<sup>3</sup> Ahmedabad Urban Development Authority and Others dated October 19, 2022

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actually carrying out such objects of GPU and the aggregate receipts from such activity do not exceed 20% of the total receipts of the institution.

In this context, the Supreme Court has dealt with certain general principles as well as dealt with each category of institution and the brief summary is as follows:

- An institution carrying on object of GPU cannot engage itself in any trade, commerce or business; however, in the course of achieving the object of GPU, it can carry on trade, commerce or business, subject to the activity being connected to the achievement of the object and subject to the cap of 20% referred to above.
- Charging of consideration for such an activity at cost or nominally above cost cannot be considered to be trade, commerce or business; the same conclusion cannot apply when the charges are markedly or significantly above cost.
- The Assessing Officer must ascertain on a yearly basis by reviewing the records to evaluate whether the nature of the assessee activities amount to trade, commerce or business and if so, whether the quantified limit referred to above has been breached, in which case the exemption shall be disentitled.

***Katalyst Comments:***

- (i) The judgement deals with various different kinds of institutions and the matter will have to be looked at separately for each.*
- (ii) There is a reference to “private trusts” in the last part of the judgement, but that seems to actually refer to public charitable trusts (and not to private trust under the Indian Trust Act 1882).*

#### **4. Madras HC<sup>4</sup>: Recovery of bad-debt taxable in the hands of the Transferee Company**

The Madras High Court held that the bad debts that has been recovered by the Transferee Company which was earlier written-off by the Transferor Companies is taxable in the hands of amalgamated company under Section 41(1) of the Act. Given that the Transferor Company had earlier claimed a deduction, irrespective of the fact that the Transferee Company had not claimed a deduction, but given the fact that the Transferee Company is a successor of the Transferor Company, it would be deemed that the Transferee Company had claimed a deduction on account of bad debt written off, which was earlier claimed as deduction by the Transferor Company, since the right to recover bad debts was transferred by the Transferor Company to the Transferee Company on amalgamation.

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<sup>4</sup> M/s Sundaram Finance Ltd v JCIT (Mad.) (T.C.A.Nos.272 & 275 of 2022)

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### 5. **Mumbai ITAT<sup>5</sup>: TP not applicable to slump sale between foreign-held Indian entities**

The Tribunal held that slump sale between two Indian Companies which are associate enterprises are not subject to transfer pricing provisions even though they are held by the same foreign company, since none of the two parties are non-residents and therefore, a domestic slump sale would not fall under the definition of “international transaction”.

### 6. **Mumbai ITAT<sup>6</sup>: Brought forward loss need not be set-off against exempt capital gains**

The Mumbai Tribunal recently held that if the capital gains on sale of shares of an Indian company was exempt as per Article 13(4) of the India-Mauritius DTAA, any other long term or short-term loss which is brought forward shall not be set off against such exempt capital gains. In other words, since the exempt capital gains was not taxable in the first place, the brought forward losses would continue to remain intact for set off against other capital gains.

### 7. **Kolkata ITAT<sup>7</sup>: Set-off of business loss against the deemed capital gains related to business**

The Kolkata Tribunal, in line with the decision of the Karnataka High Court in the case of Nandi Steels<sup>8</sup>, recently held that any short-term capital gains on sale of an asset used for business purposes should be eligible to be set off against any brought forward business loss. Ordinarily, any brought forward business loss is only eligible to be set off against business income; however, under the current circumstances, given that the income arose from sale of a business asset, but such income is merely classified under the head “capital gains”, it would not render that such income did not arise from business, even though not classified under the head “profits or gains from business or profession”, and therefore, brought forward business loss should be eligible to be set off against capital gains on sale of business asset u/s 72(1)(i) of the Act.

### 8. **Bangalore ITAT<sup>9</sup>: Recharacterization of preference shares as debt not permissible**

The Bangalore Tribunal, rejecting the contentions of the tax authorities, recently held that recharacterization of preference shares as debt, and taxing the redemption premium on a time-accrual basis as “interest” is not tenable. The legal nature of any financial instrument should duly be considered for taxation, and therefore, redemption premium would only be taxable as capital gains in the year of redemption and not on time-accrual basis.

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<sup>5</sup> MWH India Pvt Ltd v DCIT (Mumbai ITAT) (ITA No 1891/Mum/2014)

<sup>6</sup> ACIT v M/s J. P. Morgan India Investment Company Mauritius Limited (Mumbai ITAT) (ITA No 2382/Mum/2021)

<sup>7</sup> Infinity Infotech Park Ltd v Pr CIT (Kolkata ITAT) (196 ITD 316)

<sup>8</sup> Nandi Steel Ltd v. ACIT (Kar.) (128 taxmann.com 267)

<sup>9</sup> Enzen Global Solutions Pvt. Ltd v ITO (Bangalore ITAT) (ITA No 2332/Bang/2019)

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### 9. **CBDT: Extension of time limit of modified return under Section 170A of the Act**<sup>10</sup>

As per Section 170A of the Act, which came into effect on April 1, 2022, entities undergoing business reorganization (merger, demerger, etc.) can file modified returns within 6 months from end of the month in which the said order was issued so as to give effect of business reorganization. To facilitate filing modified returns (i.e., under Form ITR-A) for reorganizations concluded between April 1, 2022 and September 30, 2022, the time period has been extended to March 31, 2023.

### B. Corporate Law/ IBC Highlights

#### 1. **NCLT<sup>11</sup>: Consent affidavit would not deprive any aggrieved party to approach NCLT later**

The NCLT allowed the Petitioner Companies to dispense with the meetings of shareholders and creditors of the companies on the basis of consent affidavits submitted by the Petitioner Companies. However, NCLT have stated that it would be open for any person who is interested in the Scheme of Arrangement to put forth their contentions at any point in time before NCLT despite dispensation given for not convening meeting of equity shareholders and creditors.

#### ***Katalyst Comments:***

*This decision would unnecessarily make the process of any merger/ demerger burdensome if there are objections received by the shareholders/ creditors, notwithstanding the fact that the shareholders/ creditors would have consented to the merger/ demerger after perusing various facets and documents of a particular merger/ demerger.*

#### 2. **NCLT<sup>12</sup>: CICs with less than Rs 100 Crores are not required to obtain registration from RBI**

In connection with the Scheme of Amalgamation, the Regional Director observed that the Petitioner Company should be liable to be registered as an NBFC since more than more than 50% of its income and assets is financial income and financial assets respectively. However, accepting the submission by the Petitioner Companies, the NCLT held that if such companies are “Core Investment Companies” (i.e., 90% of its assets are investments in group companies, and 60% is in the form of equity shares), then such CICs would not be required to be registered with RBI if either such companies have not accepted public funds or its total assets are less than INR 100 Cr. This is in line with the Master Direction on CICs issued by the RBI<sup>13</sup>.

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<sup>10</sup> CBDT order under Section 119 dated September 26, 2022

<sup>11</sup> M/s Pious Electronics Pvt Ltd & Others CA (CAA) NO. 05/230/HDB/2022 (NCLT Hyderabad)

<sup>12</sup> Ambition Towers Pvt Ltd & Others C.P. (CAA) No. 65/KB/2022 (NCLT Kolkata)

<sup>13</sup> Paragraph 6 of the Master Direction - Core Investment Companies (Reserve Bank) Directions, 2016

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### 3. **Supreme Court<sup>14</sup>: Erstwhile Promoters cannot hold stake in corporate debtor under IBC**

The Supreme Court, upholding the decisions of the NCLT/ NCLAT, has held that the erstwhile promoters of the corporate debtor cannot continue to hold shares in corporate debtor as per the resolution plan approved by NCLT and they are required to sell the shares to the bidder at the value mentioned in the resolution plan under IBC proceedings.

### C. SEBI/ RBI

#### 1. **Revised SOPs issued by Stock Exchanges on Scheme of Arrangement by listed companies<sup>15</sup>**

In line with the earlier SOPs prescribed by BSE/ NSE, the following highlights the consolidated SOPs in relation to Scheme of Arrangement by listed entities:

- Submission of Scheme to seek NOC from BSE/ NSE to be submitted with 15 working days from the date of approval of the Board.
- Latest audited financials of unlisted companies to not be older than 6 months.
- For valuation, financial to not be more than 3 months old.
- The Board to consider the Scheme within 7 working days from the date of valuation
- Power to return the application and forfeit fees in case of inadequacy of documents or non-compliance of SEBI Circulars or in absence of appropriate response from the listed entity, if the same is not rectified within 7 working days by the listed entity.

#### 2. **SEBI<sup>16</sup>: Issue and listing of Commercial Paper by REIT and InvIT**

To enable REITs/ InvITs with net worth more than INR 100 Cr to issue Commercial Papers, in line with RBI Directions<sup>17</sup>, SEBI has also now allowed REITs/ InvITs to issues CPs provided that it adheres with the said RBI Directions, listing norms under under SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021, and subject to the overall debt limit prescribed under REIT/ InvIT Regulations.

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<sup>14</sup> Neeraj Singal & Anr. v. Tata Steel Ltd. & Anr. Civil Appeal No. 4654 of 2022

<sup>15</sup> BSE Notice No 20220928-13 dated September 28, 2022 and NSE Circular No NSE/CML/2022/46 dated September 28, 2022

<sup>16</sup> SEBI/HO/DDHS/DDHS\_Div3/P/CIR/2022/ 122 dated September 22, 2022 and SEBI/HO/DDHS/DDHS\_Div3/P/CIR/2022/ 123 dated September 22, 2022

<sup>17</sup> Reserve Bank Commercial Paper Directions, 2017 dated August 10, 2017

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### 3. SEBI<sup>18</sup>: Relaxations for fund raising in REIT/ InvIT

To facilitate further fund raising in REIT/ InvIT, SEBI has:

- Removed the extended period of 12 months vis-à-vis minimum listing period to make preferential allotment with institutions and has restated it to 6 months.
- Permission to sponsors to subscribe to unsubscribed portion in the institutional placement subject to 90% subscription, specific end use being acquisition of assets, lock in conditions, and permission of unitholders.

### 4. SEBI: Decisions in Board Meeting dated September 30, 2022

SEBI has approved a number of proposals; key proposals are highlighted as under:

- Disclosure of KPIs, and issue price per share based on past funding rounds, and recommendation by committee of Independent Directors that the pricing band is justified.
- Confidential pre filing of offer documents at the time of IPO filings.
- Ordinary resolution + Majority of minority approval in place of special resolution for appointment and removal of Independent Director.
- Reduction of minimum holding requirement by sponsor(s)/sponsor group(s) from 25% to 15% of REIT units to be in line with InvIT Regulations.
- Discontinuation of separate regulatory framework for unlisted InvITs.
- Dispensing the minimum 10% shareholding of non-promoter for offering shares under Offer for Sale mechanism and reduction of cooling period from +/- 12 weeks to a range of +/- 2 weeks to +/- 12 weeks.
- Acquirer carrying the open offer under Takeover Code may now have an option to provide unconditional and irrevocable bank guarantee for the entire consideration (subject to RBI approval) as against existing requirement of deposit cash.
- Inclusion of trading in units of Mutual Funds under Insider Trading Regulations.

### 5. RBI<sup>19</sup> : Identification of NBFC Upper Layer companies - Scale based NBFC Regulations

Earlier in October 2021, RBI had sought to classify NBFCs on the basis of a scale-based approach to further enhance the regulatory framework for NBFCs vis-à-vis systemic risk. Recently, on September 30, 2022, the RBI has come out with a list of “Upper Layer” NBFCs which would be required to adhere to enhanced regulatory framework with 24 months, and would be required to be listed within a period of 3 years from September 30, 2022.

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<sup>18</sup> SEBI/HO/DDHS/DDHS\_Div3/P/CIR/2022/129 dated September 28, 2022 and SEBI/HO/DDHS/DDHS\_Div3/P/CIR/2022/130 dated September 28, 2022

<sup>19</sup> Press Release dated September 30, 2022 read with RBI/2021-22/112 DOR.CRE.REC.No.60/03.10.001/2021-22 dated October 22, 2021

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### 6. RBI: Maximum time limit on repatriation of funds remitted under LRS

Presently, resident individuals are permitted to retain or reinvest the income earned from investment made under LRS. RBI has now amended the said rules to provide that if the aforesaid amounts are not reinvested, then the same need to be repatriated within 180 days from the date of such receipt / realization / purchase / acquisition or date of resident individual returning to India.

#### ***Katalyst Comments:***

*Whether investment in bank accounts to earn minimum base interest in a foreign account would be considered as “reinvestment” is not apparent from the above.*

### 7. RBI: Concept note on Introduction of digital Rupee (e₹)

RBI has introduced the concept of Central Bank Digital Currency (CBDC) referred to as e₹ (digital Rupee). The e₹ will provide an additional option to the currently available forms of money. It is substantially not different from banknotes, but being digital it is likely to be easier, faster and cheaper. It also has all the transactional benefits of other forms of digital money.

## D. Goods and Service Tax highlights

### 1. Bom HC<sup>20</sup>: Disputed GST can be paid by utilizing amount from electronic credit ledger

The Bombay High Court has held that the amount payable before filing an appeal can be paid by way of utilization from electronic credit ledger, relying on a CBIC Circular<sup>21</sup>.

### 2. TN AAR<sup>22</sup>: No ITC w.r.t. installation of solar power plant since output exempt

The Tamil Nadu AAR recently held that since electricity generated through solar panels in exempted from being considered as output provision of good/ services (in the context of captive use), input tax credit availed on installation of solar panels would not be available.

### 3. Allahabad HC<sup>23</sup>: Refund of amount due to technical error in e-way Bill

The Allahabad High Court recently permitted refund of amount collected merely on account of non-mentioning of vehicle number in e-way Bill, which is a technical error at best, since there were there were no allegations of non-payment of tax and intention to evade the tax.

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<sup>20</sup> Oasis Reality vs UOI & Ors [TS-493-HC(BOM)-2022-GST]

<sup>21</sup> CBIC Circular No. 20001/2/2022-GST dated July 6, 2022

<sup>22</sup> In the matter of VBC Associates [TS-498-AAR(TN)-2022-GST]

<sup>23</sup> Citykart Retail Pvt Ltd v. The Commissioner Commercial Tax U.P. [TS-483-HC(ALL)-2022-GST]



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### **4. Clarifications<sup>24</sup> regarding availment of ITC and credit note set-off for F.Y.2021-22**

The CBIC has clarified that the extended time limit upto November 30, 2022 is applicable for availment of ITC and credit note set-off for F.Y.2021-22.

### **5. GST on ocean freight and air freight at the time of export of goods**

GST Exemption on ocean freight and air freight at the time of export of goods was available upto September 30, 2022. Until it is clarified, GST on ocean freight and air freight at the time of export of goods would be payable by the shipping lines @5% and by airlines @ 18% on forward charge basis as per notification no. 11/2017-CGST (Rate) dated June 28, 2017.

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<sup>24</sup> Press release by Ministry of Finance on October 4, 2022