KATALYST
ADVISORS

Katalyst Kaleidoscope

September 2021: Tax and Regulatory Insights

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A. Income Tax highlights

1. Government releases draft of declaration to be given by companies to enable withdrawal of retrospective tax demands vis-à-vis indirect (offshore) transfers

The Government has passed the Taxation Laws (Amendment) Act, 2021 ("TLAA") in Parliament on August 13, 2021 to amend the indirect transfer tax provisions u/s 9 of the Income-tax Act, 1961 ("Act") making them prospective, i.e. from May 28, 2012. Broadly, section 9(1)(i) of Act was amended with retrospective effect from 1 April 1961 vide Finance Act, 2012, providing for levy of capital gains on transfer of shares, by a non-resident, of, inter alia, a foreign company which derives its value substantially from an Indian company or assets. However, with the amendment u/s 9 of the Act vide the TLAA, the said indirect transfer tax provisions have now been, effectively, made prospective (with effect from May 28, 2012). With respect to the transfers made prior to May 28, 2012 and which have been subject to any litigation, the TLAA stipulates certain conditions to be fulfilled by the taxpayers to be eligible to have the litigation withdrawn and the tax amount deposited be refunded.

The significant aspects of the draft rules have been discussed below:

Process to be followed/relevant forms:

- **Form 1:** Declarant (taxpayer) to furnish an undertaking in the specified format within 45 days
- **Form 2:** Tax authorities will accept (by granting certificate) or reject (by passing an order) such undertaking of the Taxpayer within 15 days
- **Form 3:** Taxpayer to withdraw, discontinue or waive any proceedings and furnish an intimation within 60 days
- **Form 4:** Tax authorities to pass an order, giving directions to either grant or not grant relief to the Taxpayer, within 30 days
- Tax authorities to give effect to the direction of the above order and issue refund (if any), revoke attachments (if any), and withdraw appeals and proceedings relating to such indirect transfer matter

Undertakings to be furnished by the Declarant and the Interested Party[1] (if any)

- Where any proceedings pertaining to the relevant order[2] are pending:
    - to irrevocably withdraw, discontinue and not to pursue the said proceedings, and

[1] Interested Party shall include all the holding companies in the entire chain of holding, as defined under the Companies Act, 2013, of the Declarant and the persons (including third parties) whose interest may be affected (directly or indirectly) by the undertaking.

[2] Order (including assessment order, rectification order, order deeming a taxpayer in default for not withholding taxes) passed by the income-tax authorities with respect to the income accruing or arising from the indirect transfer of shares undertaken before May 28, 2012

    - to irrevocably terminate, release, discharge, waive, etc. any existing or future right, claims, demands, liens, costs, etc. arising out of or in any way relating to the imposition of tax, interest and/ or penalty based on the relevant order.

- Where no proceedings pertaining to the relevant order are pending:
    - no proceedings have been initiated and will be initiated, or
    - after initiation of the proceedings, the same have been irrevocably withdrawn and will not initiate in the future.

Other significant aspects to be considered

- The Declarant (taxpayer) is required to indemnify the Indian Government of all costs and expenses, if any other interested party of the Declarant makes any claim against the Indian Government at any time after filing the undertaking.
- The Declarant is required to issue a press release announcing the signing of the undertaking.
- Any dispute with respect to any forms or orders or directions issued under the draft rules shall be governed by the Indian laws.

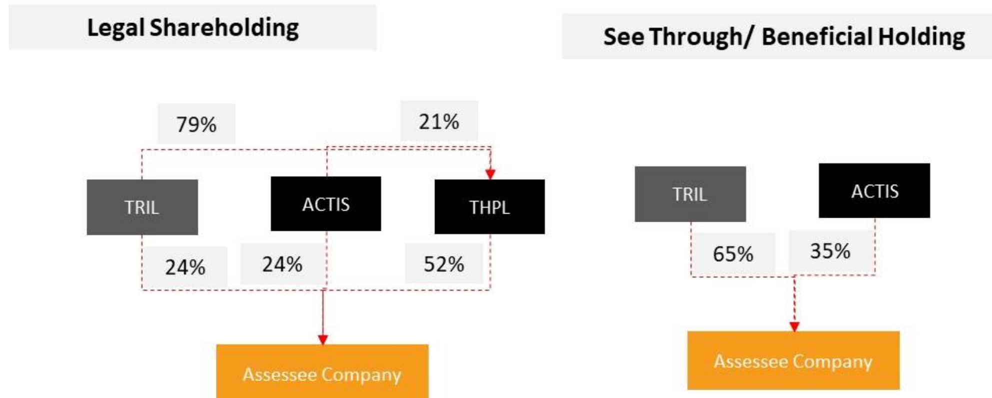
Katalyst Comments:

While it has taken nine years for the government to reverse the infamous retrospective taxation, the withdrawal of the same has, indeed, set a right message to foreign investor. However, given that the investors would only be refunded the principal amount (and not interest thereon) and given that the refund would be in INR, from a commercial perspective, it would entail a significant forex loss to the investor in addition to the enormous management time which would have been invested to fight out the litigation.

2. Mumbai ITAT: Set-off of losses under Section 79 to be allowed if there is no effective change in management and voting rights of the company[3]

In the given case, the Assessee-company had declared total income as Nil for AY 2014-15, after setting off brought forward loss of ~INR 4.98 crores. As on 31 March 2013, three companies (i.e. TRIL, ACTIS and THPL) held 100% stake in the Assessee-company, inter-se between these three companies. Incidentally, THPL was in turn held by TRIL and ACTIS and therefore, beneficially the assessee company was directly or indirectly held by THPL and ACTIS. This can be represented diagrammatically as follows:

[3] Tril Roads Private Limited [TS-843-ITAT-2021(Mum)]



Therefore, TRIL held ~65% directly or indirectly in the Assessee Company. There was a change in shareholding in FY13-14 of the assessee company, as a result of merger of THPL with TRIL and transfer of stake in the assessee company held by ACTIS to TRIL, as a result of which TRIL held 100% stake in the assessee company as on 31 March 2014. Legally, TRIL's stake increased from 24% to 100%, while beneficially, it increased from 65% to 100%.

Consequently, given that the beneficial ownership/ voting power did not change in excess of 51% (i.e. since TRIL continued to hold more than 51% both in FY12-13 and FY13-14), the provision for lapse of brought forward losses u/s 79 were not triggered merely because of change in legal ownership. However, the tax authorities contended that the brought forward losses lapsed on account of change of legal ownership from 24% to 100%.

Upholding the contentions of the assessee company, the Mumbai ITAT observed that there is no change in the management as well as "voting rights" in the assessee-company. TRIL controlled the management directly (as well as indirectly) at the time of incurring losses, and continued to control post-merger. Effectively, all companies were a part of the same group, and the whole group is managed by the same set of directors and shareholders. Accordingly, ITAT allowed set-off of brought forward of losses to the assessee-company relying on the fact that TRIL was controlling and having beneficial ownership of 65% (24% directly and 41% indirectly)..

Katalyst Comments:

The decision of the Delhi High Court in the case of Yum Restaurants (India) P. Ltd[4] is distinguishable from the present case since, in the case of the former, the beneficial ownership did not remain the same. However, the Mumbai Tribunal by upholding the concept of "lifting the corporate veil" has favourably interpreted the provisions of section 79, thereby, validity the

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[4] Yum Restaurants (India) P. Ltd. v. ITO [2016] 380 ITR 637 (Del)

concept of substance over form and also providing clarity on intra-group restructurings which do not result in change in management or change in beneficial shareholding.

3. Mumbai ITAT: Tax planning, timing of transaction and commercial prudence – loss on share sale held eligible for set off on facts[5]

The facts were that the assessee individual, an NRI, had a capital gain of approximately INR 95 lacs from sale of property and had also made a loss of ~ INR 1.11 crore from sale of certain shares of a private limited company. The revenue disallowed the loss set off on the basis that the latter transaction seemed fictitious.

The ITAT noted that the shares in the private limited company were practically worthless and there was clearly a loss to the assessee; it further went on to hold that while there was some tax planning involved, "it is not for the Assessing Officer to take a call on how should an assessee organise his fiscal affairs so as to serve the interests of the revenue authorities. This transaction may be tax-motivated, but that factor does not, by itself, render the transaction a sham transaction or a colourable device".

The ITAT relied on the SC ruling in McDowell & Co. and has stated that "It is not the tax planning simplicter, but tax planning through dubious methods or colourable devices which has been deprecated by Their Lordships in the aforesaid observations" and has quoted from SC Ruling in Vodafone International, "every tax payer is entitled to arrange his affairs so that his taxes shall be as low as possible and that he is not bound to choose that pattern which will replenish the treasury".

Katalyst Comments:

This is an important order, since it reiterates the principle that tax planning by itself cannot be the base of a disallowance; it also has relevance in the context of the legislated GAAR, in the sense that it reiterates the principle that, if the transaction is a commercial transaction with an incidental tax benefit, GAAR should not apply. However, the standard for establishing commercial justification for intra-group transactions would still be high, given the same would be related party transaction and therefore, may not be at arms' length basis.

4. Pune ITAT: Assessment order passed against non-existent amalgamating company considered it to be substantive illegality, and hence it should considered be "bad under law"[6]

In the present case, assessee company had filed return in the name of Honeywell Turbo (India) Private Limited, and it was noted that the assessee had merged with Honeywell Turbo Technologies (India) Private Limited [*later name changed to Garrett Motion Technologies*

[5] Michael E Desa [TS-874-ITAT-2021(Mum)]
[6] Garrett Motion Technologies (India) Private Limited [TS-400-ITAT-2021(PUN)-TP]

(India) Private Limited] vide order dated July 5, 2013 of Hon'ble High Court of Bombay, with an appointed date of April 1, 2012.

The tax authorities passed order under Section 92CA and Section 143(3) of the Act in the name of Honeywell Turbo (India) Private Limited on January 28, 2014 i.e. Transferor Company. The assessee had intimated to the tax authorities about the amalgamation vide letter dated September 3, 2013. Accordingly, the assessee contended that final assessment order passed by the tax authorities in the name of Transferor Company, which is non-existent as on the said date, is bad under law.

The Tax authorities contended that notice under Section 142(1) was issued in the name of Honeywell Turbo (India) Private Limited on July 3, 2013, on which date there was no order passed by the Hon'ble Bombay High Court approving the scheme of amalgamation.

The ITAT observed that assessee had informed the tax authorities about the amalgamation; however, the consequential proceedings like TP order under Section 92CA, draft order under Section 143(3) of the Act were passed by the tax authorities in the name of a non-existent transferor entity. Therefore, the issuance of "notice" in the correct name does not attain any significance in view of consequential orders passed on non-existing entity. Relying on Supreme Court ruling in case of Maruti Suzuki India Limited, the Pune ITAT concluded that final assessment order and demand notice issued in the name of non-existent entity is bad under law, and the appeal of Revenue was dismissed.

Katalyst Comments:

Pune Tribunal has rightly dismissed the Revenue's appeal in this matter, since assessment proceedings cannot be undertaken on a non-existent entity. One key point which should be borne is mind by taxpayers is that, tax authorities should be promptly informed about any restructurings / amalgamations, to avoid unnecessary litigations in future.

5. Pune ITAT: Debentures issued to shareholders should not be recharacterized as "shares", and accordingly Arm's Length Price to be determined in respect of interest paid on such debentures[7]

During transfer pricing assessment proceedings of the assessee for AY 2016-17, the Transfer Pricing Officer (TPO) observed that the assessee-company had not done proper benchmarking of payment of interest on debentures.

The TPO observed that the assessee had issued Compulsorily Convertible Debentures to its Associated Enterprises (AEs) in India and abroad, against which it had claimed an interest payment of ~ INR 3.92 crores. In respect of the same, the TPO held that the transaction was a "shareholder activity" and payment of interest was nothing but a self-inflicting loss. Further,

[7] City Corporation Limited [TS-399-ITAT-2021(PUN)-TP]

TPO also held that agreement between the lenders (who are also the shareholders) and the company was entered to avoid paying tax on dividend which would be available for distribution. Accordingly, the TPO took Arm's Length Price of the interest payment as Nil, and made an addition of INR 3.92 crores.

The Pune ITAT held that the assessee-company rightly issued debentures to its AEs and the Assessing Officer was not justified in re-characterizing the debentures as "shares". Further, ITAT restored the matter to AO / TPO for a fresh determination of Arm's Length Price on the interest payment.

Katalyst Comments:

This is an important decision which can have relevance in the context of the limitations to the tax department to re-characterize transactions. Genuineness of the transactions should be considered by the tax authorities before re-characterizing any aspect of the transaction. However, the deduction of interest would need to be looked at in the context of section 94B of the Act, which seeks to restricts interest paid to AEs in excess of 30% of the EBITDA.

6. Mumbai ITAT: Amount originally received towards allotment of shares, subsequently treated as "gift" on failure to issue shares due to non-compliance under FEMA, is not a taxable receipt[8]

Assessee-company engaged in business of ITES, received INR 3.46 crores from a Canadian company. It disclosed and credited the said amount under "Reserves & Surplus" in the balance sheet. The company could not issue shares against the money received to the Canadian company, as the Indian promoters missed the six month deadline stipulated under FEMA regulations. Accordingly, assessee-company treated the sum of INR 3.46 crores as a "gift". Tax authorities held that the receipt was treated as a gift to circumvent the FEMA provisions, and held it to be taxable which was confirmed by CIT(Appeals).

ITAT held that merely because there was a violation of FEMA regulations by not allotting shares within 6 months from the date of receipt of monies towards share capital, such amount cannot automatically become income of the assessee. Accordingly, ITAT examined the applicability of provisions of Section 28(iv) r.w. Section 2(24)(ix), and Section 56 of the Act. On applicability of Section 28(iv), ITAT observed that the monies were not received in the ordinary course of business, and accordingly held that the conditions for applicability of the Section 28(iv) are not satisfied in the instant case. With regards to taxability under Section 56(1), ITAT observed that receipt should first be chargeable under Section 2(24) to be taxable under any of the heads of income. If the said receipt is not at all chargeable to tax under any heads of income, then the said receipt cannot be chargeable to tax in terms of Section 56(1) of the Income-tax Act.

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[8] Crescent Payments Pvt. Ltd [TS-834-ITAT-2021(Mum)]

The ITAT relied on the Hon'ble Supreme Court ruling in the case of G.S. Homes & Hotels [this is an important order in the context of real income] wherein it was held that amount received on account of share capital ought not to be treated as business income, and held that the amount received by assessee should not be taxable.

Katalyst Comments:

This is an important decision issued in the context of "gift" of shares. Key takeaway from the above Mumbai Tribunal ruling is that, to determine taxability of any receipt, first it is important to determine whether such receipt is taxable under any of the heads of income in Section 14. If the said receipt does not fall under Section 14, then it shall be considered non-taxable.

7. Delhi ITAT: Interest on debentures "payable" to non-resident is not covered under Article 11 of India-Cyprus DTAA, and hence no TP-adjustment can be made on "hypothetical receivable amount" in the hands of non-resident[9]

The assessee is a company incorporated in Cyprus. The assessee had subscribed to 15% Fully Convertible Debentures (FCDs) of face value INR 100 each of 4 Indian Associated Enterprises (AEs). During AY 2009-10, 15% of above debentures were converted into 0% FCDs. The Transfer Pricing Officer held that 15% of the FCDs were converted into 0% FCDs without assigning any reason, and hence the TPO made adjustment of interest at the rate of 15% (as it was being charged prior), amounting to INR 4.02 crores.

Aggrieved by the above TP adjustment, assessee filed appeal against the CIT(Appeals), who held that the word "interest paid" as per Article 11(1) of India – Cyprus DTAA, includes "interest payable". Accordingly, CIT(Appeals) upheld the order of the TPO / AO.

However, the Delhi ITAT observed that Article 11(1) of India – Cyprus DTAA envisages that, for taxing the interest income in the hands of the non-resident, it is necessary that interest should arise in a Contracting State, i.e. twin conditions of accrual as well as payment are to be satisfied. In the given case, the TPO/AO have not been able to establish that notional interest satisfies the test of income "arising" or "received" under the charging provisions of Income Tax Act. If income is not taxable in terms of Section 4, then transfer pricing provisions cannot be made applicable, because Section 92 provides for computing the income arising from international transactions with regard to the Arm's Length Price. Only the interest income chargeable to tax can be subject matter of transfer pricing in India.

Accordingly, ITAT concluded that transfer pricing adjustment would not be applicable since interest has neither been received nor accrued to the assessee, and hence it cannot be held to be chargeable in terms of the Income Tax Act read with Article 11(1) of India – Cyprus DTAA.

Katalyst Comments:

[9] Mondon Investments Ltd [TS-384-ITAT-2021(DEL)-TP]

This is an important order in the context of real income. It has been held by various Tribunals and Hon'ble Courts (as discussed in the ruling), that the words "paid" cannot be extended "payable" in respect of interest under relevant articles under DTAA.

8. Supreme Court judgment regarding depreciation on flats used for business purpose[10]

The assessee was a partnership firm and had purchased a flat in Mumbai for business purposes in 1974; it claimed depreciation and the same was allowed for over 20 years and thereafter, the assessee discontinued claiming depreciation for 2 years, post which the flat was sold. The assessee offered the profit as long-term capital gains, but the Assessing Officer held that profit on depreciable asset is taxable as short-term capital gains under section 50.

The matter went right up to the Supreme Court, and the Supreme Court held that the flat continued to be part of depreciable assets and the non-use only disentitles the assessee for depreciation for 2 years prior to the date of sale; however, there was no provision whereby a depreciable asset being part of the block of assets can cease to be part of the block.

9. CBDT extends timelines for filing Income-tax Returns and various reports of Audit for Assessment Year 2021-22[11]

On consideration of difficulties reported by taxpayers and other stakeholders in electronic filing of income-tax returns and various other reports under the provisions of the Act, the CBDT has provided relaxation in respect of various compliances as under:

Particulars	Actual date of filing (as per Act)	First Extension (vide circular dtd. May 20, 2021)	Newly Extended dates
Income-tax Return (Non-Audit cases)	July 31, 2021	September 30, 2021	December 31, 2021
Tax Audit Report	September 30, 2021	October 30, 2021	January 15, 2022
Transfer Pricing Report	October 31, 2021	November 30, 2021	January 31, 2022
Income-tax Return (Audit cases)	October 31, 2021	November 30, 2021	February 15, 2022
Income-tax Return (Transfer Pricing applicable)	November 30, 2021	December 31, 2021	February 28, 2022
Belated / Revised Return	December 31, 2021	December 31, 2021	March 31, 2022

[10] Sakthi Metal Depot vs CIT (2021) 436 ITR 1 (SC)
[11] Vide Circular No. 17/2021 dated September 9, 2021

In the above circular, CBDT has clarified that the extension of due dates for filing of Income Tax Return shall not affect the provisions under Explanation 1 to section 234A (Interest for default in furnishing ITR), if amount of tax payable exceeds Rs. 1 lakh.

Further, CBDT has clarified that in the case of a resident individual referred to in Section 207(2), i.e. senior citizen not having any income from business or profession, the tax paid by him under Section 140A within the original due date (without extension), shall be deemed to be the advance tax.

Katalyst Comments:

This is a welcome relief provided by the Government, considering the technical hassles on the income-tax website faced by many taxpayers.

B. Corporate Law Highlights

1. Government to consider proposal to bring LLPs under CSR ambit[12]

The Government is considering a proposal to amend existing laws to make it mandatory for LLPs and state-run banks to spend 2% of their net profit in "corporate social responsibility" activities. At present, CSR spending is mandatory for companies incorporated under Companies Act, 2013, with minimum net-worth of INR 500 crores OR revenue of INR 1,000 crores OR net profit of INR 5 crores. Small companies which do not meet the above criteria are not covered under the ambit of CSR.

LLPs and public sector banks (PSBs) are governed by the LLP Act, 2008 and Banking Regulation Act, 1949 respectively, and these laws are silent on the matter of CSR. Government has observed that big corporates are taking the LLP route to avoid CSR spending.

2. NCLT order in the case of Protrans Supply Chain Management Private Limited in the context of providing exit to shareholders

In a scheme of arrangement before the Mumbai NCLT, Protrans Supply Chain Management Pvt. Ltd. and another company were to merge with a third company called Baramati Agro Ltd. One of the transferee companies had 21,676 shareholders, out of which 21,000 shareholders were holding small amount of equity shares. In this context, the scheme envisaged that these shareholders would be issued redeemable preference shares and the ROC objected to this.

[12] *Source:* Livemint news article dated August 18, 2021

The NCLT Mumbai vide order dated September 20, 2021 approved the scheme of arrangement including on the basis that the word 'arrangement' is a term of wide import and merger and demerger are not the only components of scheme of arrangement, as has been held in judicial precedents earlier.

Katalyst comments:

This is an important order in the context of providing an exit to shareholders and can be used to facilitate exit of joint venture partners, minority shareholders, family settlements, etc.

C. Securities Law Highlights

1. SEBI Board approves tighter norms relating to Related Party Transactions

SEBI, in its board meeting held on September 28, 2021[13], has approved the amendments to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 in relation to regulatory provisions on related party transactions (RPTs), which shall come into effect from April 01, 2022 (unless otherwise specified by SEBI).

Key amendments are as follows:

i. **"Related Party**" shall now include all persons and entities forming part of promoter and promoter group. Further, with effect from April 01, 2023, any person holding beneficial interest of 10% or more in the listed entity, shall also be treated as "related party". This change seeks to also cover any shareholder who may not be related to the promoter/ promoter group but holds stake in excess of 10%.

ii. Definition of "**Related Party Transactions**" has been widened to cover transactions with any person or entity, the purpose of which is to benefit a "related party" of the listed entity. Further, it has also been widened to include transactions between the listed entity or any of its subsidiaries on one hand and a related party of the listed entity or any of its subsidiaries on the other hand, as opposed to transactions only undertaken by the listed company.

iii. Prior approval of shareholders shall be required for "material RPTs" (INR 1000 crores or 10% of consolidated turnover, whichever is lower)

iv. Approval of Audit Committee under certain cases such as material modifications subsequent to the approval of the RPT, and where a subsidiary is a party to the transaction but the listed entity is not, subject to the threshold of 10% of the consolidated

[13] Press Release PR No. 28/2021 dated September 28, 2021

turnover of the listed entity, ii. 10% of the standalone turnover of the subsidiary w.e.f. April 1, 2023.

v. Enhanced disclosure of information to be provided to Audit Committee, shareholders and Stock Exchanges.

2. SEBI Board approves proposal to amend existing framework for delisting of shares pursuant to open offer

The Board of SEBI has approved the proposal to make amendments to SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("Takeover Regulations").

Under the existing framework, if an open offer is triggered, compliance with Takeover Regulations could take the incoming acquirer's holding to above 75%. However, if the delisting offer fails (i.e. 90% shareholding is not achieved), the acquirer would be forced to first bring its stake down to 75%. Such directionally contradictory transactions in a sequence pose complexity in the takeover of listed companies especially where the acquirer desires to get the company delisted pursuant to his take over.

Under the revised framework, SEBI has permitted simultaneous open offer and delisting process for the Acquirer. To protect the interest of public shareholders, the Acquirer will be required to propose of higher price for delisting with suitable premium over open offer price, if the delisting offer is accepted (i.e. acquisition of stake beyond 90%) and open offer price, if the delisting offer fails.

In case if a company does not get delisted pursuant to open offer and the Acquirer crosses 75% threshold, SEBI has provided a cushion of 12 months to make further attempts to delist the company.

SEBI has clarified that, while undertaking delisting under the revised framework, all other provisions Delisting Regulations shall continue to apply.

3. SEBI gives in-principle nod for shifting to concept of "controlling shareholders"[14]

The Securities and Exchange Board of India has given an "in-principle" nod to the proposal of shifting from the concept of "Promoter" in a listed entity to the concept of "person in control" or "controlling shareholders" in a smooth, progressive and holistic manner.

The Board noted that investor landscape is now changing with private equity and institutional investors holding significant shareholding in listed companies. Further, the Board also noted that, in recent years number of businesses and new age companies with diversified

[14] *Source:* SEBI press release PR No. 24/2021 dated August 6, 2021

shareholding and professional management that are coming into the listed space are non-family owned and/or do not have a distinctly identifiable promoter group.

Accordingly, SEBI Board has advised SEBI to:

a) engage with other regulators to ascertain and resolve regulatory hurdles, if any;
b) prepare draft amendments to securities market regulations and analyze impact of the same; and
c) further deliberate and develop a roadmap for implementation of the proposed transition.

Katalyst Comments:

There are various obligations and responsibilities on the "promoter/ promoter group", and this concept itself is a legacy of the Securities Contracts (Regulation) Act, 1956. However, with the evolving M&A space, where private equity players are increasingly acquiring controlling stake over listed entities, the concept of promoter/ promoter group may become redundant and therefore, the introduction of the concept of "persons in control" would help in identifying the shareholders who are actually running the show.

4. SEBI mandates listed entities to disclose shareholding segregated into "Promoter" and "Promoter Groups"[15]

SEBI vide circular dated August 13, 2021 has notified revised format for statement showing shareholding pattern of the Promoter and Promoter Group.

In the interest of transparency to investors, all listed entities are now required to provide shareholding pattern segregated into "Promoter" and "Promoter Group".

The revised format of the disclosure table is provided in Annexure A of the above-mentioned circular.

5. SEBI amends LODR to mandate higher disclosures on "high value" debt-listed companies

SEBI has notified the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Fifth Amendment) Regulations, 2021[16] wherein certain provisions which were previously applicable only to equity listed entities, will now be applicable to certain "high value" debt listed entities.

Key takeaways of the amendment are as under:

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[15] SEBI circular SEBI/HO/CFD/CMD/CIR/P/2021/616 dated August 13, 2021
[16] Notification No. SEBI/LAD-NRO/GN/2021/47. dt. September 7, 2021

- NCD-listed entities having outstanding value of listed NCDs of INR 500 crores or more as on 31 March 2021 will have to comply with Corporate Governance Provisions of LODR. These entities will be referred as "High Value Debt Listed Entities"
- All listed entities with non-convertible securities shall now submit financial results on a quarterly basis (earlier half yearly)
- Enhanced intimation and disclosure requirements for all entities with listed non-convertible securities

Katalyst Comments:

The above notification has certainly raised compliance requirements for debt-listed entities, which could be a burden for such companies. However, by notifying the above, SEBI has raised the bar on corporate governance standards for companies resorting to only listing of debt issuances, and virtually bringing them on par with the compliances already laid down for equity listing by companies.

6. SEBI issues consultation paper on Review of SEBI (Settlement Proceedings) Regulations, 2018

The concept of settlement proceedings/consent terms was introduced through a SEBI Circular in 2007, and thereafter, these evolved into Settlement Regulations in 2014 and subsequently into the captioned settlement regulations.

The Consultation Paper dated September 14, 2021 mentions that, on the basis of experience gained from dealing with settlement applications, SEBI believes that it is necessary to refine these regulations and has proposed several changes therein. Incidentally, it may be noted that the Settlement Regulations provide for settlement under these regulations in relation certain violation/alleged violations by persons (which would include promoters, listed companies, market intermediaries such as brokers and merchant bankers), asset management companies, etc. against whom "specified proceedings" have been initiated by SEBI.

They key amendments proposed to the Settlement Regulations are as follows:

- Limitation period for filing settlement application proposed to be restricted to 60 days from the date of issue of the show cause notice, as against 180 days currently.
- Time period for submission of revised settlement terms after the meeting of SEBI's internal committee proposed to be restricted to 15 days, instead of 20 working days currently.
- Time limit for remittance of settlement amount proposed to be restricted to 30 days, instead of an aggregate 90 days currently.
- "Proceeding conversion factor" which is a factor which is the basis for arriving at the ultimate settlement amount is prescribed in the regulation is currently as 0.65 to 1.20 of the base value; it is proposed to amend it to 0.45 to 1.50.

- Mitigating or aggravating factors are currently applied to the base value only once; the proposal is to have the ability to apply it more than once, but subject to a maximum limit of 3.
- Provisions with regard to disclosure of violation under Takeover Regulations and Insider Trading Regulations are arrived at on the basis of base amounts; in the context of system driven disclosures and other factors, the amounts are intended to be rationalised to reflect the evolving nature of the regulatory landscape.
- A distinction is intended to be made between peripheral and non-peripheral entities, the latter often being dummy directors, mule account holders etc. It is proposed that non peripheral entities would be subject to lesser penalties.

Katalyst Comments:

The provisions are extremely prescriptive and leave very little scope for either the SEBI internal committee or High Powered Advisory Committee (HPAC) to exercise discretion. While discretion has its own downsides, in practice, an over prescriptive regime can lead to unintended and absurd results, including very high penalties.

Regulation 5(2) of the Settlement Regulations provides a carve out that certain alleged defaults may not be settled. These carve outs are very subjective, in the sense that they refer to terms such as "market wide impact", "causing loss to large number of investors", or "affecting the integrity of the market". There need to be guidelines, so that the carve out is not used to reject several matters that can be settled, as opposed to being embroiled in endless litigation.

7. SEBI issues circular explaining modalities for implementation of the framework for "Accredited Investors" under the SEBI (Alternate Investment Fund) Regulations

The Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 (AIF Regulations) were amended on August 3, 2021 (Third Amendment) and August 13, 2021 (Fourth Amendment) which has primarily introduced the concept of 'Accredited Investors' and granted certain relaxations for Alternative Investment Funds (AIFs) with Accredited Investors.

SEBI has laid down the modalities for implementation of the framework of "Accredited Investors" vide circular dated August 26, 2021[17].

Under the aforesaid framework, Accredited Investors (AIs) may avail flexibility in minimum investment amount ("Lower ticket size") or concessions from specific regulatory requirements applicable to investment products, subject to conditions applicable for specific products/ services under the aforesaid Regulations.

[17] SEBI Circular No. SEBI/HO/IMD/IMD-I/DF9/P/CIR/2021/620

SEBI has laid down certain criteria which should be fulfilled by persons to be considered as "Accredited Investors". Mainly it includes minimum net worth criteria (>INR 7.5 crore) and annual income criteria (>INR 2 crore) for individuals / HUFs. Similarly, for body corporates, minimum net-worth criteria of INR 50 crores should be satisfied.

Persons desirous of being reckoned as AIs shall approach an Accreditation Agency for accreditation. Accreditation Agencies shall be mainly responsible for verification and timely processing of applications, maintain data of AIs, etc. The following entities are eligible to carry out accreditation process:

i. Subsidiaries of Recognized Stock Exchanges, provided the Stock Exchange meets certain criteria relating to minimum net-worth, presence in India, etc.
ii. Subsidiaries of Depositories

In addition to the above, the aforesaid Circular captures detailed steps and procedure for Accreditation.

Katalyst Comments:

The segregation of categories of investor is, in principle, a good step and is helpful in reducing over presumptive and highly regulative investment.

D. Foreign Exchange Management Act, 1999

1. Government amends FEMA to ensure that FDI in private banks having investment in insurance sector to be addressed to RBI for consideration

The Ministry of Finance issued a notification[18] to bring amendments relating to FDI in insurance sector by notifying Foreign Exchange Management (Non-debt Instruments) (Second Amendment) Rules, 2021 ("the said Rules").

Earlier this year the Government had amended the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 to enable the increase in foreign direct investment limit in the insurance sector to 74 per cent.

According to the said Rules, applications for FDI in private banks having joint ventures or subsidiaries in the insurance sector may be addressed to the Reserve Bank of India for consideration in consultation with the Insurance Regulatory and Development Authority of India, to ensure that the limit of foreign investment of 74 per cent for the insurance sector is not breached.

[18] Notification S.O. 3411(E) dated August 19, 2021

E. Insolvency & Bankruptcy Code, 2016

1. IBBI releases discussion paper to propose amendments to strengthen regulatory framework of liquidation process

The Insolvency and Bankruptcy Board of India released a discussion paper on August 27, 2021 on issues pertaining to "accountability of liquidator", "sale of assets" and "security interest" with a view to strengthen regulatory framework of liquidation process.

IBBI proposes that liquidator shall consult Stakeholder's Consultation Committee (SCC) for all significant matters relating to the liquidation process, including appointment of professionals (and their remuneration) and sale of assets (including fixation of reserve price, manner of sale, etc.) to reduce information asymmetry. However, the liquidator shall have the ultimate authority to take decisions.

Further, IBBI suggests that Schedule I of the Liquidation Regulations should be modified to explicitly prohibit the appointment of agents/professionals for sale of assets (during the liquidation process) on commission or success fee basis, and that the liquidator shall prepare a marketing strategy for sale of assets of the Corporate Debtor in consultation with the SCC.

IBBI also adds that in order to address the issue of arbitrary rejection of highest bid, it is proposed that the liquidator shall provide the reasons for rejection of the highest bid to the highest bidder, and record the same in the quarterly progress report.

Lastly, in furtherance of resolving the impasse regarding relinquishment or realization arising in cases where multiple secured creditors have *pari-passu* charge over assets of the Corporate Debtor, the IBBI recommends that if the secured creditors having 60% of the value in the secured debt decide to relinquish or realize the security interest, such decision shall be binding on the other *pari-passu* charge holders.

2. CBDT amends Income-tax Rules to align with Insolvency & Bankruptcy Code

CBDT vide Notification No. G.S.R. 578(E) dated August 18, 2021 amended the Income-tax Rules to allow resolution professionals appointed by the National Company Law Tribunal (NCLT) to verify the tax returns of the companies undergoing bankruptcy.

The Income-tax (24th Amendment) Rules, 2021 notified by the tax department has also made it the obligation of the Resolution Professional to follow the rules meant for tax return preparers of certain assessees. Authorized representatives who prepare tax returns for assessees are required to furnish details of the documents given by the assessee for preparation of the return as well as details of the scope and findings of any examination the representative has done on such documents.

As per the amendment, the new rules authorize the Resolution Professional to furnish this information in the case of a company undergoing bankruptcy proceedings.

3. Landmark Supreme Court judgment in the case of Jaypee Kensington Boulevard Apartments Welfare Association versus NBCC (166 SCL 678) – COC powers and related issues

The Supreme Court in the case of Jaypee Kensington Boulevard Apartments Welfare Association versus NBCC vide a judgement dated March 24, 2021 in the context of the Insolvency & Bankruptcy Code 2016 (IBC Code) has dealt with a large number of issues in a landmark judgement. Here is a summary of some of the key aspects of the judgement:

- There is no scope for interference with commercial aspects of a decision of the Committee of Creditors (COC). If the NCLT finds any shortcoming in the resolution plan submitted, it can only send the resolution back to the COC for resubmission; in a scheme of IBC, the resolution plan is exclusively in the domain of the commercial wisdom of the COC.

- The COC can simultaneously consider more than one resolution plan at the same time and vote on electing one of the available options; there is no prohibition in the scheme of the IBC that COC cannot simultaneously consider and vote upon more than one resolution plan.

- If the home buyers have assented to a resolution plan, any individual home buyer or association of home buyers cannot maintain a challenge on the resolution plan and cannot be treated as a "dissenting financial creditor".

In the process envisaged by the IBC, where the COC may approve a resolution plan by a vote of not less than 66%, obviously there is a possibility that some of the financial creditors are not voting for approval and they could be conveniently defined as dissenting financial creditors. The NCLT, however, had rejected the submissions sought to be made by a few home buyers, who asserted themselves to be dissenting home buyers because the authorized representative on behalf of the home buyers had assented to the resolution plan. The NCLT had observed that the dissenting home buyers cannot be considered as dissenting financial creditors. The Supreme Court confirmed the order of the NCLT on this aspect.

F. Goods and Service Tax Highlights

1. Transfer of business from Airport Authority of India ('AAI') to Special Purpose Vehicle ('SPV') is a 'transfer of going concern' and exempt from GST

AAI conducted a bidding process wherein Adani Enterprises Ltd. won the bid of airport quoting highest bid among all agreeing to form a SPV for operation, management and development of the airport which include civil, mechanical, electrical works, terminal buildings, cargo facilities, runway and all other project asset for a lease period of 50 years. In this regard, the Gujarat

Authority of Advance Ruling[19] ('AAR') has held that transfer of business as going concern by the AAI to SPV is classified as 'supply' as per the provisions of section 7 of the CGST Act, 2017 and said supply is exempt as per serial no. 2 of notification no. 12/2017-CT dated June 28, 2021.

Katalyst Comments:

A welcome ruling by the Gujarat AAR whereby transfer of business on going concern basis by way of lease period of 50 years has been classified as exempt supply. The AAR has clarified that the transfer of going on concern is not limited to sale (i.e., slump sale/Itemised sale) but such transfer may be witnessed in other circumstances such as lease, licences, gift.

2. Challenge to constitutional validity of section 54(3) of the CGST Act and Rule 89(5) of the CGST Rules dismissed and refund under inverted duty structure available for inputs and not for input services

The Hon'ble Apex court[20] or the Supreme court ('SC') dismissed the challenge to constitutional validity of section 54(3) of the CGST Act and Rule 89 (5) of CGST Rules with a finding that absence of the words "as may be prescribed" in Section 54(3) does not deprive the rule making authority to make rules for carrying out the provisions of the Act. Further, the Apex court rejected assesee's argument to broaden the expression 'inputs' to cover both goods and services with a remark that "To construe 'inputs' so as to include both input goods and input services would do violence to the provisions of Section 54(3) and would run contrary to the terms of Explanation-I". Also, on the vires of Rule 89(5) vis-à-vis Section 54(3), SC rejects assessee's submission that Rule 89(5) goes beyond the provisions of the Act when in the garb of fixing a formula, it restricts the refund of ITC to input goods by denying ITC of input services. The Court however noted the anomaly with regard to the formula prescribed under Rule 89(5) and directed GST council to reconsider the formula to compute GST refund due to practical inequalities attached to it and also clarified that formula is not ambiguous.

Katalyst Comments:

In this judgment, the Apex court has held that in case of inverted duty structure, refund is admissible only with respect to inputs and not for input services. The court has overturned the judgment of Gujarat High court in the same case VKC Footsteps India Pvt. Ltd. v. Union of India[21] which was is in favour of Assessee and upheld the Madras High court judgment in the case of Tvl. Transtonnelstroy Afcons Joint Venture v. Union of India[22] which was in favour of Revenue

[19] In the matter of Airport Authority of India [TS-461-AAR(GUJ)-2021-GST]
[20] UOI & VKC Footwear & Others [TS-472-SC-2021-GST]
[21] [TS-472-SC-2021-GST]
[22] [TS-596-HC-2019(PAT)-NT]

3. ITC reversal is required if entitlement of ITC is in excess of what is prescribed under rule 36(4) of the CGST Rules, 2017

Under this, the supplier furnished FORM GSTR-1 and FORM GSTR-3B pertaining to the period Jan to March 2020 in the month of November, 2020 which restricted ITC in the auto-drafted FORM GSTR-2B of the Applicant for the month of November'20 with the remark 'Return Filed Post Annual Cut-off'. In this regard, the West Bengal AAR[23] has held that based on the provisions of section 16 read with Rule 36 (4) of the CGST Rules, the details of the invoices in respect of such supplies have not been uploaded by the supplier during the said tax periods and the ITC in respect of the same has been availed by the Applicant and hence, it is in violation of restrictions as prescribed in Rule 36(4) of CGST Rules, 2017.

Katalyst Comments:

The AAR has not considered the fact that the service recipient has paid GST and filed GST return in time. However, due to failure of service provider in filing of GST returns in time, the ITC benefit has been rejected to the service recipient. This issue should be settled by way of necessary amendment under the GST Law.

4. In case of transfer of development rights by the landowner to the developer under Joint Development Agreement('JDA'), GST is payable by the developer on the date earlier of completion date or first occupancy

The Tamil Nadu AAR[24] has held that in case of transfer of development rights by the landowner to the developer under JDA, GST is payable by the developer at the time earlier of completion date or first occupancy as per notification no. 11/2017-CT (Rate) dated June 28, 2017 as amended by notification no. 3/2019-CT (Rate) dated March 29, 2019. Further, value to be adopted for construction service shall be deemed to be equal to the Total Amount charged by the developer for similar apartments in the project from the independent buyers, other than the person transferring the development rights nearest to the date of transfer of development rights as provided vide sr no. 2A of notification no. 11/2017-CT dated June 28, 2017 as amended by notification no. 3/2019-CT dated March 29, 2019.

5. Key recommendations – 45th GST council meeting held on September 17, 2021 – to be effective from a date to be notified

[23] In the matter of Eastern Coalfields [TS-468-AAR(WB)-2021-GST]
[24] In the matter of Thiru Neelakanta Realtors Ltd. Liability [TS-470-AAR(TN)-2021-GST]

a. **Concession on specified Goods** – GST rates reduced from 12% to 5% for medicines used for cancer treatment and concession extended till December 31, 2021 for COVID related drugs
b. **E-commerce Aggregators** – Liable to GST as under:
   i. Transport of passengers, by any type of motor vehicles through it w.e.f. 1st January, 2022
   ii. Restaurant services provided through it with some exceptions w.e.f. 1st January, 2022.

c. **E-invoicing: - N**o need to carry the physical copy of tax invoice in cases where invoice has been generated from einvoice portal having IRN;

d. **Interest on ineligible ITC availed and utilised -** Section 50(3) of the CGST Act to be amended retrospectively, w.e.f. 01.07.2017, to provide that interest is to be paid by a taxpayer on "ineligible ITC availed and utilized" and not on "ineligible ITC availed"

e. **Transfer of unutilised CGST and IGST balance** - Unutilized balance in CGST and IGST cash ledger may be allowed to be transferred between distinct persons (entities having same PAN but registered in different states), without going through the refund procedure.

f. **GST on royalty paid on mining rights –** The services by way of grant of mineral exploration and mining rights attracted GST rate of 18% w.e.f. 01.07.2017.

6. Circular[25] on intermediary services

The Government has clarified that a person incorporated in India under the Companies Act, 2013 and a person incorporated under the laws of any other country are to be treated as separate legal entities and would not be barred by the condition (v) of the sub-section (6) of the section 2 of the IGST Act 2017 for considering a supply of service as export of services.

Further, it is also clarified that provisions of section 13 of IGST Act can be invoked only when either the location of supplier of intermediary services or location of the recipient of intermediary services is outside India.

Katalyst Comments:

A very important clarification for BPO and IT sector; Group companies or subsidiaries companies incorporated in India will be treated as separate entities from their foreign parent

[25] Circular no. 159/15/2021-GST dated September 20, 2021

companies/group companies and will be eligible for export status for exports to their foreign parent companies/group companies.

Our Offices:

Mumbai
71/75 Mittal Tower,
7th Floor, C Wing,
Nariman Point,
Mumbai - 400021
Tel: +91 22 4917 1616

Pune
#406-408,
Global Square, Near Bund-Garden,
Yerwada, Pune- 411006
Tel: +91 20 4840 7700