

## Devadhaantu Insights – December 2020



Dear Reader,

Greetings!

We are happy to present the Devadhaantu Insights highlighting important legislative updates in direct taxes and regulatory updates in SEBI.

We hope that we are able to provide an insight into various updates that you would find to be informative as well as useful.

Happy Reading!

Devadhaantu Advisors

**Thank You**

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# DIRECT TAX UPDATES

DECEMBER 2020



## Direct tax updates (1/6)

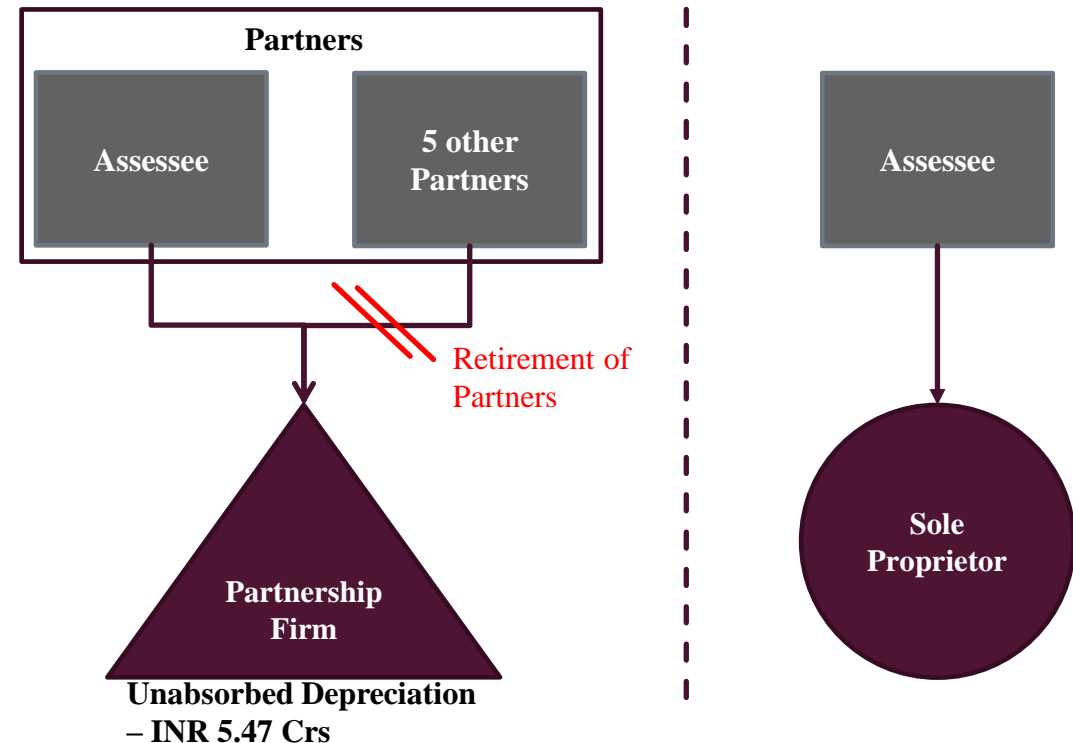
### Unabsorbed depreciation of dissolved firm allowable to successor proprietorship<sup>1</sup>

Assessee was partner in a partnership firm, alongwith 5 other partners, who retired from the firm leaving capital assets of the firm undistributed. As a result, Partnership firm was dissolved and business of the firm was succeeded by the assessee in his individual capacity.

AO disallowed the set off of brought forward depreciation of INR 5.47 Crs stating that no provisions allows carry forward of unabsorbed depreciation of a dissolved firm to an Individual.

Relying on the Supreme Court Decision in case of A. Dharma Reddy<sup>2</sup> and Madras High Court Decision in case of N. Krishnammal<sup>3</sup>, Hyderabad ITAT in the instant case held that the assessee continued the business of the firm as a successor-in-buisness, in his individual capacity. **Accordingly, unabsorbed depreciation of current year in the year of succession is allowed to be set off against the income of individual successor.**

### Structure upon retirement of Partners



<sup>1</sup> Yerram Venkata Subba Reddy (ITA No. 1119/Hyd./2018) dated 4 November 2020

<sup>2</sup> A.Dharma Reddy (1969) 73 ITR 751 dated 19 February 1969

<sup>3</sup> N. Krishnammal 147 ITR 431 dated 3 August 1982



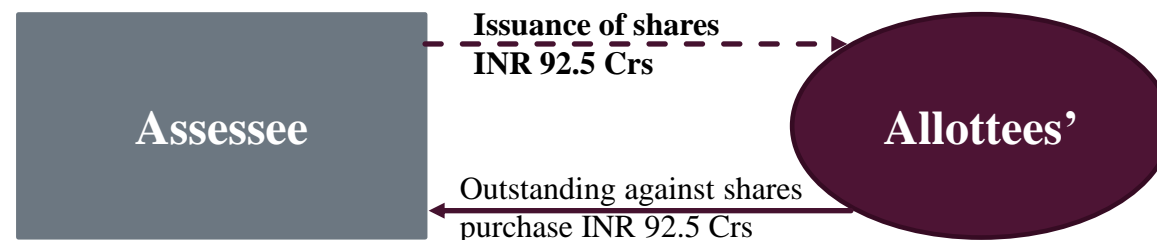
## Direct tax updates (2/6)

### Issuance of shares against book adjustment not an unexplained cash credit u/s 68<sub>1</sub>

Assessee Company had issued share capital worth INR 92.5 crores at premium to various companies. Such Companies had sold shares of other companies to Assessee and consideration towards such shares was outstanding in the books of Assessee Company. Assessee Company issued shares in lieu of such outstanding amount in the books of Assessee Company. Revenue made an addition of INR 92.5 Crs as unexplained cash credit u/s 68.

Kolkata ITAT acknowledge the fact that there was no real inflow of cash involved in the transaction and only adjustment by way of journal entries. Relying on decision of High Court in case of Jatia Investment Co., ITAT held **that addition u/s 68 was not invocable as issuance of shares was made by way of adjustment through journal entries and no cash flow was involved.**

### Allotment of shares against outstanding liability





## Direct tax updates (3/6)

### Where members of AOP are taxed at MMR, AOP is not liable to tax<sup>1</sup>

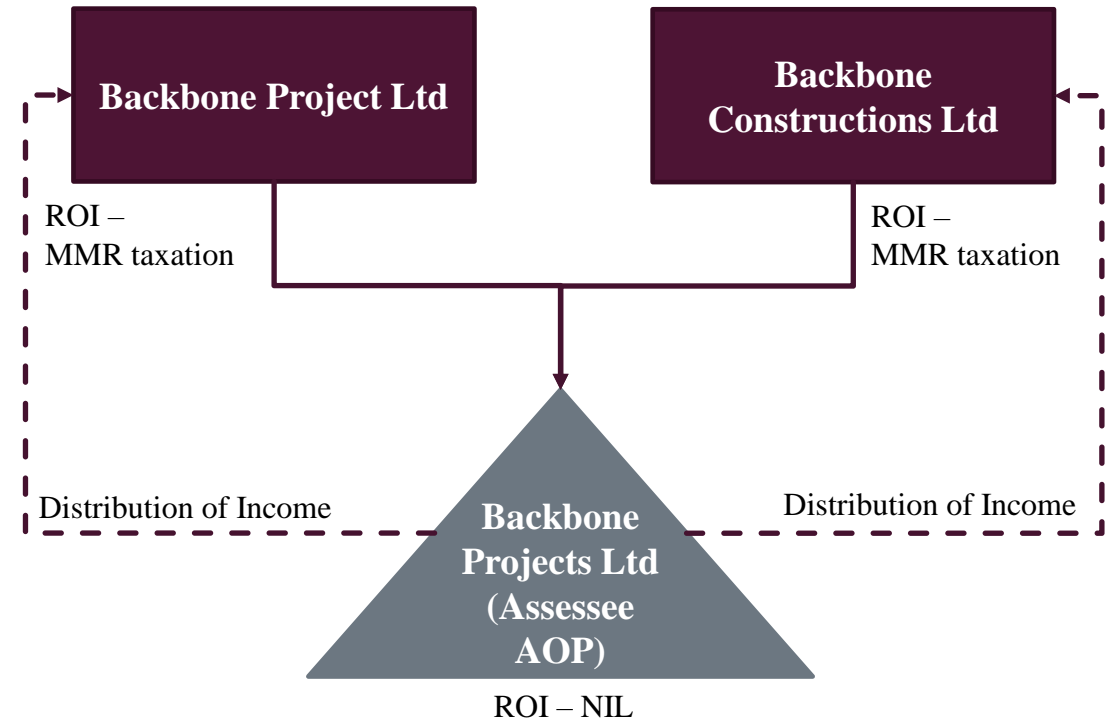
Assessee was a joint venture between Backbone Project Ltd and Backbone Constructions Ltd constituted through a Joint Venture Agreement and having a status of AOP. Gross business receipt as declared by assessee AOP were distributed to its members at its participation ratio. Assessee AOP declared NIL income in return of income filed and claimed TDS as refund. Members of the Assessee AOP shown their share of income in their Return of Income and paid taxes thereon.

Ahemedabad High Court, by placing reliance on CBDT Circular No. 7/2016, **stated held that there will not be any tax liability on the income of the joint venture if same is offered to tax by its members.**

Considering AOP was chargeable to tax at MMR and members also offered their share at MMR to tax, there was no loss to the revenue.

In light of above, Supreme Court dismissed the Special Leave Petition against High Court's order, upholding the ruling of the High Court.

### AOP – Distribution of Income



<sup>1</sup> Backbone Projects Ltd. TS-595-SC-2020 dated 19 November 2020



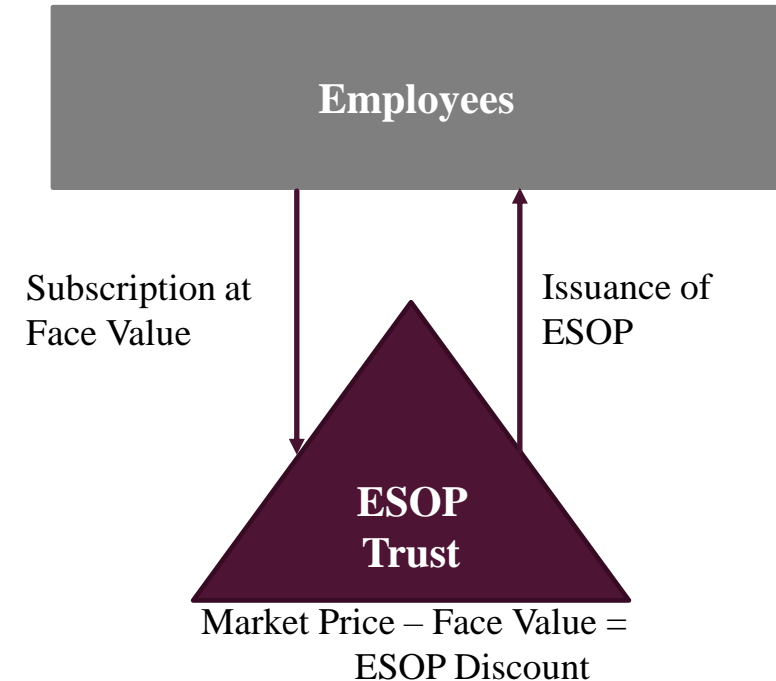
## Direct tax updates (4/6)

### Discount on ESOP issuance is allowable business expense u/s 37<sup>1</sup>

Assessee Company floated Trust for the purposes of issuance of ESOP for its employees under Employee Stock Option Plans Scheme. Under the Scheme, shares of the Assessee Company were transferred to Trust at face value. Employees were given option to buy shares within stipulated timeframe. The difference between market price and allotment price was claimed as deduction u/s 37.

Karnataka High Court reaffirmed the principle laid down by other high court and held that discount on issue of ESOP is deductible expenditure u/s 37 on following grounds:

- For claiming business expenditure, there is no requirement of pay out of expenditure in cash;
- Discount on issuance of ESOP is not contingent Liability but is an ascertained liability
- The term 'Expenditure' also includes 'Loss'.





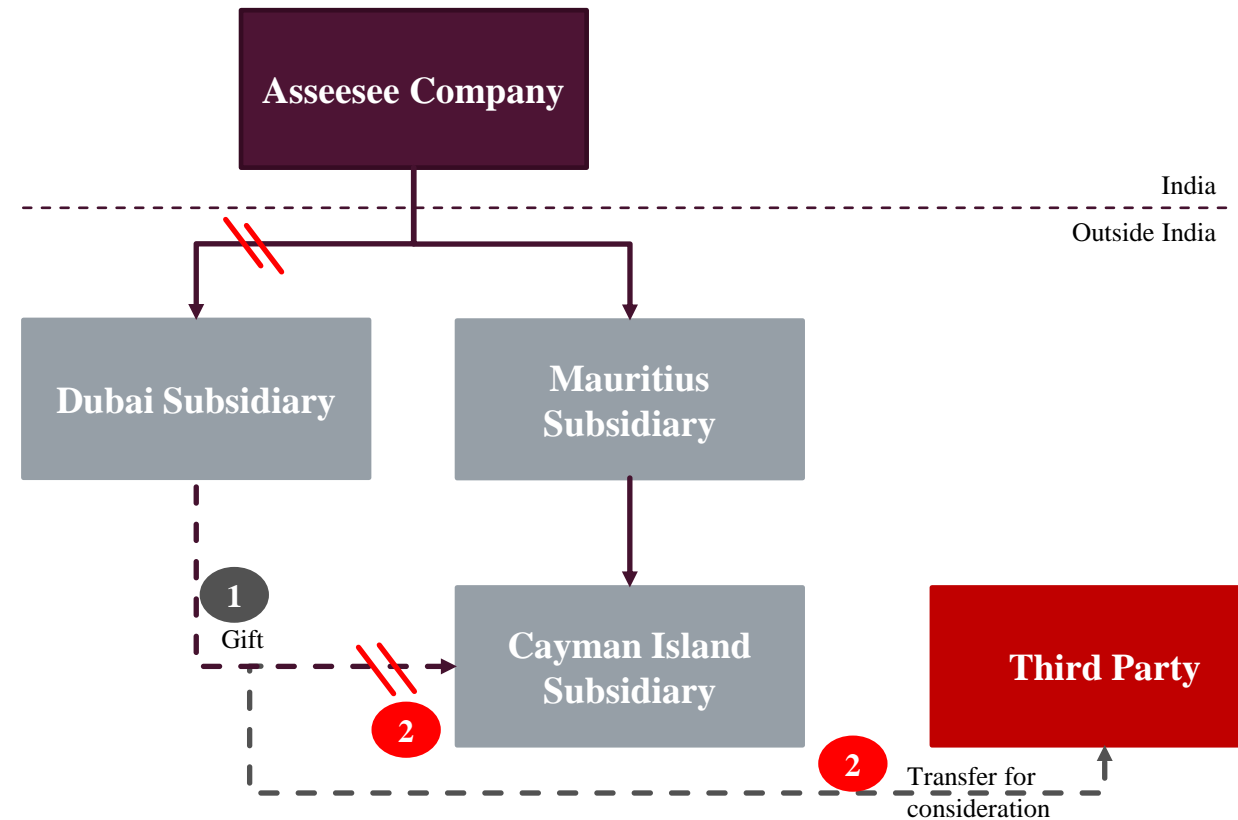
## Direct tax updates (5/6)

**Transfer of a wholly owned subsidiary to another wholly owned subsidiary followed by immediate sale to third party not considered as ‘Gift’ and held taxable transaction.**

Assessee gifted (by way of transfer) its wholly owned subsidiary incorporated in Mauritius 4 years ago to another newly incorporated step down wholly owned subsidiary incorporated in Cayman Islands. Within just 4 days of such gift, 27.17% stake in such WOS at Mauritius was further transferred to third party for a consideration by WOS at Cayman Islands.

Madras High Court held that the transaction of transfer was not merely a gift to subsidiary company under section 47(iii) of the ITA. The High Court observed that since a step-down subsidiary was created by assessee in a tax haven to act as a conduit to escape rigour of Indian Tax Laws and sole intention of assessee was for corporate re-structuring, transaction was in fact transfer of capital asset by assessee to its subsidiary and the same would be liable to tax under section 45.

### Transaction flow for transfer of subsidiary through newly incorporated step-down subsidiary



1 Redington (India) Ltd. [2020] 122 taxmann.com 136 (Madras) dated 10 December 2020



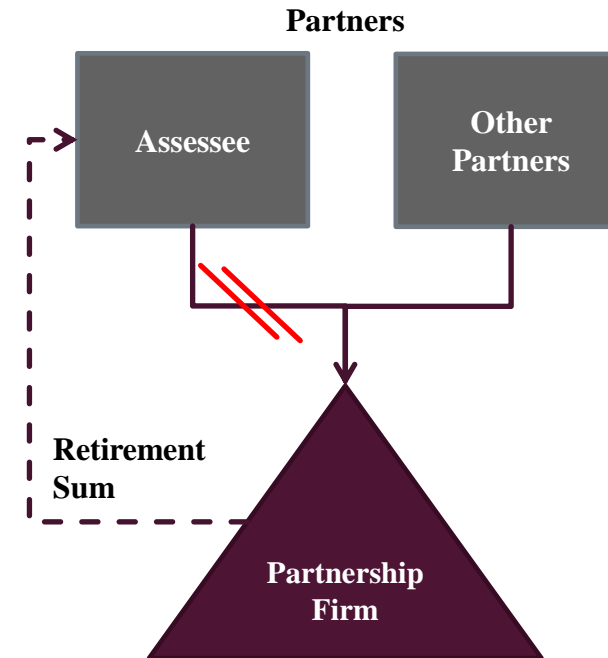
## Direct tax updates (6/6)

### No tax implications in the hands of partners upon sum received on retirement from the partnership firm<sup>1</sup>

Assessee received INR 48 Crores upon retirement from the partnership firm as the settlement of assessee's rights, title, and interest. Such sum was claimed by assessee as exempt income. Revenue held that assessee gave up his development and possession right over the plot of land which amounted to transfer of a capital asset and, as a consequence, revenue assessed the retirement benefit as Long-term Capital gains in the hands of the assessee.

In view of ratio laid down by Supreme Court and High Courts under similar facts, Mumbai ITAT held that **amount of money received on retirement by assessee from the Partnership firm is neither in lieu of capital asset, nor a 'transfer' within the meaning of section 2(47) of Income Tax Act, 1961 ('ITA')**.

### Retirement from Partnership Firm





# SEBI REGULATORY UPDATES

DECEMBER 2020



## SEBI Regulatory updates (1/2)

SEBI in its board meeting (PR No. 61/2020 dated 16 December 2020), has taken several decisions including following:

Eligibility and condition	Existing Regulation	Relaxation	Condition
<b>Listed Companies going for further issuance of equity shares and / or Convertible Equity instruments</b>	<ul style="list-style-type: none"> <li>• Minimum public shareholding of 20% of proposed issue size or 20% of post issue capital</li> <li>• Lock –in Requirement of 3 years for minimum contribution and 1 year for contribution over and above minimum contribution</li> </ul>	<b>No such conditions would be applicable for issue of equity and / or convertible equity instrument</b>	<b>Shares of the issuing company shall be frequently traded on the stock exchange</b>
<b>Listed Companies Going through Corporate Insolvency Resolution Process</b>	In case, if public shareholding falls below 10%, such listed companies are required to bring back the public shareholding to atleast 10% within 18 months, to 25% within 36 months	Such companies will be mandated to have at least 5% public holding (as against no minimum requirement at present), and the shareholding should go up to 10% within 12 months and to 25% within 36 months	<b>NA</b>



## SEBI Regulatory updates (2/2)

### Single login e-voting facility for demat account holders

[SEBI/HO/CFD/CMD/CIR/P/2020/242 dated 9 December 2020 ]

At present, there are multiple e-voting service providers ('ESPs') providing e-voting facility to listed entities which necessitates registration on various ESPs and maintenance of multiple user IDs and passwords by shareholders. Further, SEBI observed that the participation by the public non-institutional shareholders / retail shareholders is at negligible level.

In the context of the above, SEBI, vide circular dated 9 December 2020, proposed new mechanism to facilitate e-voting to all the demat account holders, by way of a single login credential, through their demat accounts / websites of Depositories / Depository Participants.

Under Phase I, shareholders can **directly register with depositories wherein they would be able to access the e-voting page of various ESPs through the websites of the depositories without further authentication by ESPs**. Alternatively, demat account holders will have the option of accessing various ESP portals directly from their demat accounts. After this, they would be routed to the webpage of the respective depositories from their demat accounts, which in turn would enable access to the e-voting portals of various ESPs without further authentication.

Under Phase II, in order to further enhance the convenience and security of the e-voting system, the depository will have to **validate the demat account holder through a One Time Password (OTP) verification process**.