

Devadhaantu Insights – October 2020



Dear Reader,

Greetings!

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

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

OCTOBER 2020



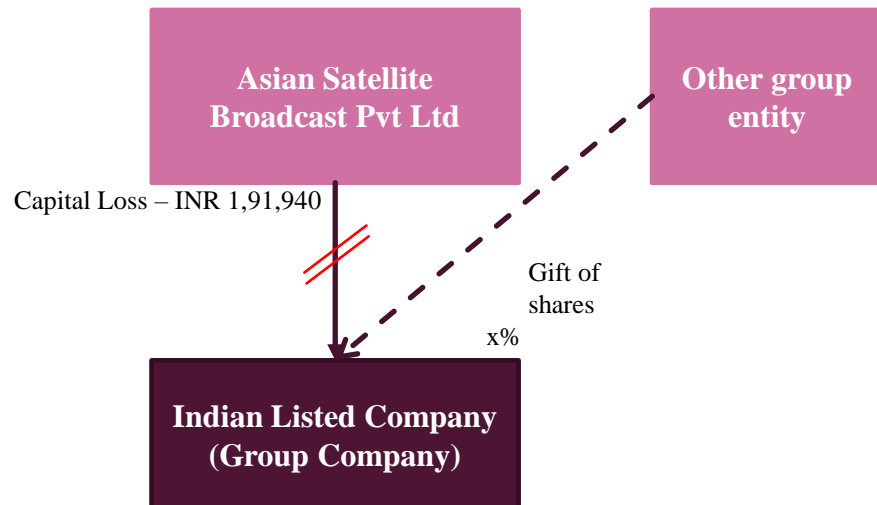
Direct tax updates (1/6)

Corporate gift under internal restructuring is exempt and not liable to capital gains tax¹

In AY 2012-13, Assessee had transferred its holding in a group company (listed) to its associate company as a part of internal restructuring. Assessee had claimed loss in the profit and loss accounts towards cost of acquisition of shares in such group company. However, none of such losses were claimed while filling tax return.

AO observed that transfer of shares of listed entity at nil consideration amongst unlisted group entity was made with the sole purpose of evading payment of capital gains tax and such transfer fell within the scope of a colourable device and worked out capital gains at INR 3.36 crs.

Restructuring Arrangement



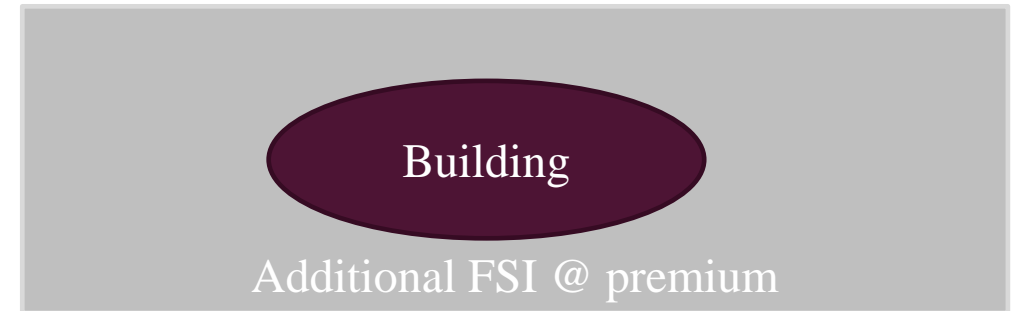
The Assessee contented that these shares were gifted via a board resolution and there was no requirement of a gift deed and there is no provision in the law which prohibits a company from giving or receiving gifts. Further, there was no embargo on a company to gift any property in order for a “transfer” not to be considered as a transfer exigible to capital gains tax u/s u/s 47(iii) of the Income Tax Act (“ITA”). In light of the above, **the Bombay High Court held that fair market value of shares gifted by a company cannot be liable to capital gains tax owing to a specific exemption u/s 47(iii) of the ITA.**



Direct tax updates (2/6)

FSI eligible for depreciation claim, akin to that of building and not of intangible asset

The assessee had acquired certain rights in the form of additional Floor Space Index (“FSI”) over and above the existing FSI, subject to payment of premium. However, this premium was to be paid under an installment scheme. On payment of first installment, assessee received the rights in the form of additional FSI which was capitalized in the books of account and a corresponding credit entry was made as a liability to be paid. This was also reflected in the balance sheet as the balance premium amount was shown as liability. This was categorized as “intangible rights” by the assessee company and a depreciation of 25% was claimed on it as the FSI would entitle the assessee to construct extra floors which would in turn increase the value of the property. The Tribunal held that the depreciation allowable would be on rates applicable to building only i.e., @ 10% and not @ 25% for some kind of intangible right. This view was upheld by the Bombay High Court.



Additional FSI Classified as intangible rights



As additional FSI would enable building of extra floors, which would in turn increase the value of property, it needs to be classified same as building and depreciation rates @ 10% would be applicable

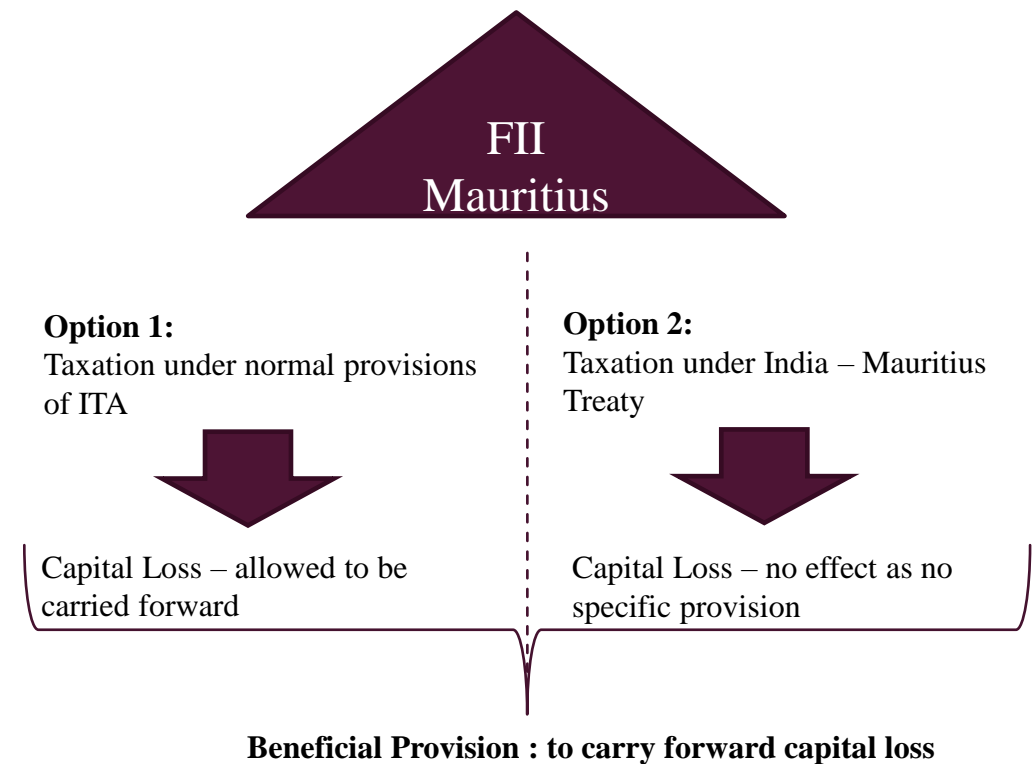


Direct tax updates (3/6)

FII eligible to carry forward capital loss, even though nature of capital loss is that of exempt under DTAA

The assessee company was a tax resident of Mauritius and was registered with the Securities and Exchange Board of India (“SEBI”) as a Foreign Institutional Investor (“FII”). The assessee company had claimed carry forward of past long-term capital losses in its return of income. The AO was of the view that when, pursuant to the India Mauritius Tax Treaty, the capital gains were not chargeable to tax in India, the assessee was neither required to show income under that head in its return, nor entitled to file a return showing capital losses merely for the purpose of getting the same carried forward to the subsequent years. This view of the AO was upheld by the Dispute Resolution Panel (“DRP”). Therefore, in effect, the carry-forward and set off of capital losses was not permitted by the AO.

On further appeal, the Tribunal concluded that the assessee was fully justified in claiming the carry forward of the capital losses. Accordingly, the Tribunal permitted carry forward of capital losses under the provisions of the domestic ITA, even though capital gains may be exempt under Article 13 of the India – Mauritius. The Tribunal relied on the basic premise that the assessee company could claim benefit for carry forward of capital losses under the domestic ITA, while continue to claim exemption from capital gains under the relevant DTAA, and that the assessee company cannot be compelled to first set off the capital losses against the capital gains.



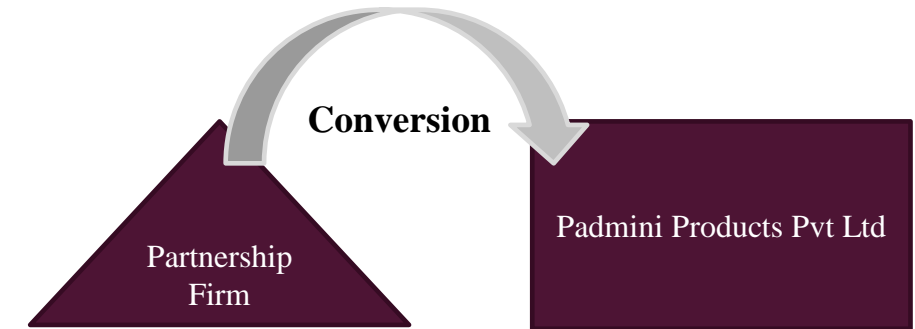


Direct tax updates (4/6)

Depreciation allowed on revalued assets upon succession of partnership firm into company

The Assessee, a private limited company, engaged in the manufacturing, dealing and export of incense sticks had succeeded a partnership firm. Before the firm was converted into a company, the assessee had revalued all its assets and liabilities including the intangibles and accordingly, shares were issued to all the partners of the erstwhile firm, as consideration. The assessee company then filed its return of income along with a depreciation claimed on the intangibles. The claim was rejected by the AO on the grounds that the assessee had neither purchased/acquired the intangible assets from any third party nor incurred any actual cost. This view was upheld by the Tribunal.

On further appeal, the High Court held that, it was a well-established fact that the partnership firm was the registered owner of various trademarks. Further, the valuation at the time of succession was done taking into consideration the necessary applicable accounting standards, which was accepted by the AO. The assessee and the erstwhile partnership firm were different entities and there was transfer of intangible assets by the partnership firm to the assessee for a valuable consideration, being allotment of shares even though the succession itself was exempt from capital gains tax u/s 47(xiii) of the ITA. Thus, the High Court, interestingly, held that depreciation should be allowable on the revalued amount, given that the revaluation was already done prior to the succession and not upon succession and therefore, the sixth proviso to section 32(1) which restricts aggregate depreciation in the hands of the successor, was not applicable in the present case.



Revaluation upon conversion of Partnership Firm into Company

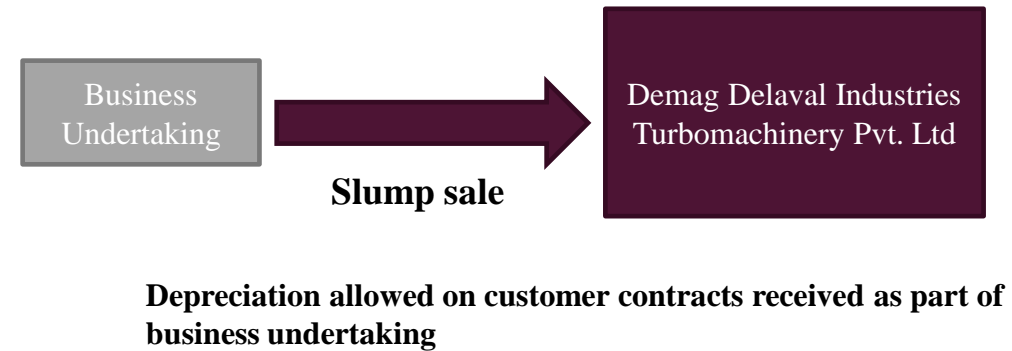
- Depreciation claimed on self generated trademark recorded upon revaluation in the books of converted private limited company
- As consideration in the form of shares was issued to the partners which included revaluation quantum, depreciation on entire revalued intangible asset was allowed and not only proportionate



Direct tax updates (5/6)

Depreciation allowed on customers contract received as part of business undertaking received pursuant to slump sale

The Assessee Company had acquired the industrial steam turbines business of Alstom Siemens AG for a purchase consideration of INR 26 Crs. This purchase consideration has been allocated to fixed and intangible assets at fair values based on an independent valuation carried out by valuers. The Assessee Company had claimed depreciation on the customer contracts acquired under slump sale categorizing them as “business or commercial rights of similar nature”. This contention was rejected by the lower tax authorities as well as the CIT(A). However, the ITAT held that the depreciation is also available on business or commercial rights of similar nature and therefore, remitted the matter back to AO to re-examine depreciation on customer contracts being akin to goodwill.

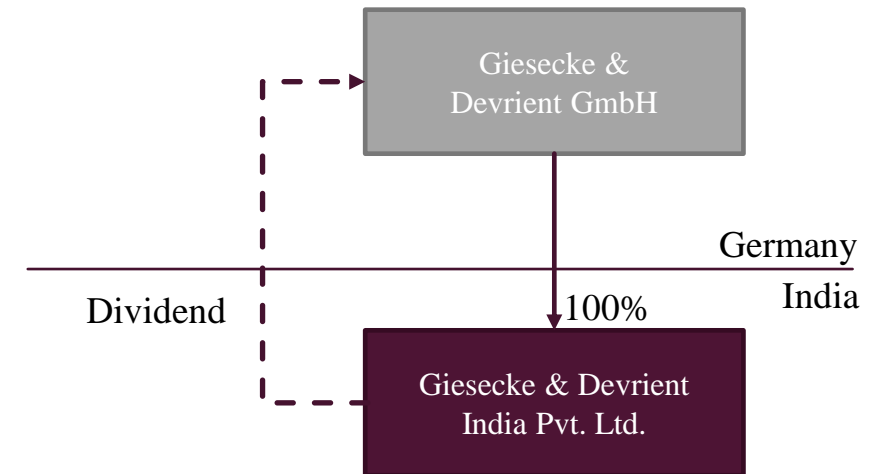




Direct tax updates (6/6)

DDT on dividend declared to foreign shareholders restricted to rates mentioned in the DTAA

The Assessee Company was a wholly owned subsidiary of a German Parent, Giesecke & Devrient GmbH. The assessee had raised an additional ground whether the Dividend Distribution Tax (“DDT”) levied in terms of section 115-0 of the ITA should be restricted to the rate of tax on dividends as provided in the applicable DTAA governing non-resident shareholders. The ITAT admitted the additional ground raised by the assessee and held that the liability to DDT under the ITA which falls on the company may not be relevant when considering applicability of rates of DDT set out in the tax treaties. The generally accepted principles relating to interpretation of treaties in the light of object of eliminating double taxation did not bar the application of tax treaties to DDT. ITAT however, remanded the matter back to AO for the limited purposes of verifying that German parent was not carrying on business in India through a Permanent Establishment in India and shareholding in the Indian Company is effectively connected to the Permanent Establishment.



CORPORATE LAW UPDATES

OCTOBER 2020

Corporate Law updates



Presidential assent accorded to the (Indian) Companies (Amendment) Act, 2020

The (Indian) Companies (Amendment) Act, 2020 has brought about certain significant changes.

Key changes of such amendment are as under:

- a. Decriminalizing several offences;
- b. Permitting the listing of Indian companies overseas;
- c. Reduction in time limit for rights issue to be kept open, so as to enable faster completion of the issue process;
- d. Certain unlisted companies having exposure to public funds to file periodic financial statements;
- e. Credit for the amount spent in excess of 2% for CSR activities to be carried forward to subsequent years;
- f. Fixed remuneration to Non-executive directors and Independent directors even in a situation when the companies have made inadequate profits or no profits;
- g. Establishing additional benches of the National Company Law Appellate Tribunal ('NCLAT')

SECURITIES AND EXCHANGE BOARD OF INDIA (‘SEBI’) UPDATES

OCTOBER 2020



SEBI Regulatory updates (1/2)

Informal Guidance issued by SEBI on contra trade restrictions and Take-over code restrictions

The applicants are the promoters of the listed company HEG Ltd. ('the Company') and they wish to undertake inter se transfer of certain number of shares of the company amongst the promoter & promoter group (i.e. between individual and non-individual insiders) by way of block deal executed on the stock exchange. The proposed inter se transfer of shares amongst the Promoter & Promoter Group shall not exceed 5% and the acquirers are non-individual members of the promoter group. RSWM Limited and other members of the Promoter & Promoter Group traded/sold certain number of shares in the open market during September 2019 i.e. 6 months prior to filing this interpretative letter with the SEBI. RSWM Limited is not a party to the current transaction.

The SEBI responded that the contra-trade restrictions apply to the promoters individually and not the entire promoter group. Insofar as the any obligation to make an open offer is concerned, since in the current transaction the shares proposed to be transferred do not exceed 5%, there would be no open offer. Therefore, the question of an exemption under the Take Over Code would not arise.



SEBI Regulatory updates (2/2)

SEBI revises FAQs on Insider Trading

Q1. Whether requirement of pre - clearance is applicable for exercise of employee stock options?

A1. No

Q2. Whether trading in ADRs and GDRs by employees of Indian companies who are foreign nationals is covered under provisions of PIT Regulations on code of conduct?

A2. Yes, In order to make any disclosures by such designated persons, a unique identifier analogous to PAN may be used.

Q3. What information should a listed Company maintain in its structured digital database, in case the designated person is a fiduciary or intermediary?

A3. Details of Unpublished Price Sensitive Information ('UPSI') and the details of persons with whom such UPSI is shared (along with their PANs/other unique identifier) and details of persons who have shared the information.

Q4. In case a designated person resigns, what information should be collected by the company/ intermediary/ fiduciary under PIT Regulations?

A4. All information which is required to be collected from designated persons, should be collected till the date of service of such employees with the company. Upon resignation from service of designated person, a company/ intermediary/ fiduciary should maintain the updated address and contact details of such designated person. These need to be updated and maintained for one year after resignation from service. Such data should be preserved for a period of 5 years.

RESERVE BANK OF INDIA ('RBI') UPDATES

OCTOBER 2020



RBI Regulatory updates

Reservations of the Enforcement Directorate ('ED') cannot prevent the RBI from allowing a company to make remittance to its foreign subsidiary

The Petitioner Company ('the Company') had sought permission from the RBI through its concerned AD Banker to remit funds to its wholly owned subsidiary overseas. These funds were to be utilized by the said overseas subsidiary to meet their financial commitments towards foreign lenders failing which the overseas subsidiary would have defaulted in meeting its overseas financial obligations. This permission was rejected by the RBI owing to pendency of investigation/enquiries under the PMLA and FEMA as expressed by the ED to the RBI.

The High Court held that the RBI needs to exercise its discretion bearing in the mind the erstwhile permissions it had granted to the company with respect to the FEMA ODI Regulations. Further, bearing in mind the facts and circumstances pertaining to the company, the RBI cannot hold the reservations by the ED as a base so as to not grant permission for remittance.

INSOLVENCY AND BANKRUPTCY BOARD OF INDIA (‘IBBI’) UPDATES

OCTOBER 2020



IBBI Regulatory updates

The Insolvency and Bankruptcy Board of India (“IBBI”) issues Use of Caveats, Limitations and Disclaimers in Valuation Reports Guidelines, 2020

With a view to make the valuation reports issued more sacrosanct from the point of view of the Registered Valuer (“RV”) and also in the interest of credibility of the RVs, the IBBI has issued certain guidelines vide a press release (“Guidelines”). These Guidelines have been issued in exercise of the powers under Rule 14(i) the Companies (Registered Valuers and Valuation) Rules, 2017 which provides a comprehensive framework for development and regulation of the profession of valuers, and have set standards of professional conduct and performance for the valuation profession in the interest of stakeholders.

These Guidelines shall be applicable on all the valuation reports to be finalised by RVs on or after October 1, 2020. Broadly, these guidelines are divided into 3 sections which are as follows:

- Need for Caveat, Limitations and Disclaimers;
- Guidance note on Caveat, Limitations and Disclaimers;
- Asset-Class wise samples of Caveat, Limitations and Disclaimers

These Guidelines provide guidance to the RVs in the use of caveats, limitations, and disclaimers in the interest of credibility of the valuation reports. These also provide an illustrative list of the caveats, limitations, and disclaimers which shall not be used in a valuation report.