Devadhaantu Insights – June 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!

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Thank You

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DIRECT TAX UPDATES

JUNE 2020

Direct tax updates

AAR denies benefit under India-Mauritius DTAA ('Treaty') to Mauritian entities on indirect transfer of shares of Indian Entity[1] (1/2)

The seller companies ("applicant companies") are private companies incorporated in Mauritius, holding Category 1 Global Business License and are tax residents of Mauritius for the purposes of the Treaty. The seller companies invested in a Singapore company which further invested in multiple Indian companies and thereby derived value substantially from its investments in India.

As a part of larger global transaction, the applicant companies proposed to transfer the shares of Singapore company to a Luxembourg based entity. The applicant companies approached the Indian tax authorities under Section 197 of the Income Tax Act, 1961 ('the Act') to seek a nil withholding certificate which was denied by the tax department on the ground that the applicant companies allegedly did not exercise independence in their decision making and therefore were not eligible to avail benefits under the Treaty. The applicant companies thereafter filed applications before the AAR under Section 245Q(1) of the Act to determine the taxability arising upon transfer of shares of Singapore company under the Act read with Treaty provisions.

The AAR rejected the application of the applicant companies on the premise that the transaction was designed for avoidance of tax, basis the following observations:

- While computing capital gains, not only the sale of shares but also the purchase of shares is relevant and therefore, the entire transaction of acquisition as well as sale of shares as a whole has to be looked and a dissecting approach of examining only the sale of shares cannot be adopted;

- 'Notes to Financial Statement' of the applicant companies states that the principal objective of the applicant companies was to act as an investment holding company for a portfolio investment domiciled outside Mauritius. The AAR further noted that the applicant companies had not made any investment other than investment in the Singapore Company. Although the holding-subsidiary structure might not be conclusive proof of tax avoidance, the purpose for which the subsidiaries were set up does indicate the real intention behind the structure and AAR therefore concluded that the real intention of the applicant companies was to avail the benefit of the Treaty.

[1] Tiger Global International II Holdings (116 taxmann.com 878) [2020]

Direct tax updates

AAR denies benefit under India-Mauritius DTAA ('Treaty') to Mauritian entities on indirect transfer of shares of Indian Entity (2/2)

- 'Control and management' do not mean day to day affairs of the business but would mean the 'head and brain' of applicant companies. In the given case, AAR referred to the minutes of the board meetings and observed that the key decisions were taken by the non-resident Director. Further, AAR noted that authority to operate the principal bank account was with US-based director who was also authorized signatory for sellers' immediate parent company, a director of the ultimate holding companies of the seller companies and was also declared as the beneficial owner of the seller companies. Accordingly, AAR concluded that the 'head and brain' of the applicant companies was not situated in Mauritius but was situated in USA.

- The holding structure of the applicant companies coupled with control and management are the relevant factors for determining the design for tax avoidance and therefore the applicant companies were only a 'see through' entities set up to avail benefits of the Treaty.

- Further, AAR also applied the yardsticks laid down by Apex Court[2] in case of Vodafone International Holding BV and concluded that in the absence of any direct investment in India nor any taxable revenue generated in India, the said arrangement was a pre-ordained transaction which was created for tax avoidance purpose. Lastly, AAR also held that since the sale involved shares of a Singapore company, the benefit provided under Article 13(4) of the Treaty will not be available to the applicant companies by concluding that the objective of India-Mauritius DTAA was to allow exemption of capital gains on transfer of shares of Indian company only and any such exemption on transfer of shares of the company not resident in India, was never intended by the legislator.

2 Vodafone International Holdings B.V. v. UOI (2012) 341 ITR 1/204 Taxman 408/247 CTR 1/66 DTR 265/6 SCC 613/Vol. 42 Tax L R 305 (SC)

Direct tax updates

Setoff of loss of demerged company allowed on filling revised return after receipt of intimation u/s 143(1) to resulting company[1]

Assessee had entered into demerger arrangement whereby upon filling of a joint petition before the High Court for approval of scheme of arrangement of a specific division of the demerged company was proposed to be demerged into the assessee company with effect from a retrospective appointed date. Pending approval of demerger from the High Court, the assessee company filed its return of income before its statutory due date without taking demerger into account. However, pursuant to the scheme of demerger approved by the High court, the assessee company filed a revised return of income for the said assessment year showing "nil" income and claimed the set-off of brought forward losses and unabsorbed depreciation of the demerged division. However, the revised return of income was filed after receipt of intimation u/s 143(1).

The assessing officer rejected assessee company's set-off claim and rejected revised return filed by the assessee company.

On appeal, CIT(A) allowed the appeal of the assessee company. On further appeal by CIT(A) to Tribunal, the Tribunal noted that the conditions stipulated u/s 72A(4) read with section 2(19AA) of the Act were fulfilled and therefore, the assessee company was eligible to claim set-off of brought forward losses pertaining to the demerged division by placing reliance on the Apex Court decision[2].

Further, the Tribunal held that the right to file revised return of income does not lapse with the issuance of intimation u/s 143(1) and such an intimation cannot be said to be "completion of assessment" and more so, when assessment has subsequently been completed under section 143(3) of the Act. The Tribunal placed reliance on the Apex Court decision[3] and concluded that the tax officer was bound to accept the revised return filed by the assessee pursuant to the scheme of demerger sanctioned by the High Court.

1 ACIT vs Padma Logistics & Khanji Pvt Ltd (ITA No. 606/Kol/2018)
2 Marshall Sons & Co. (India) Ltd. v. ITO (1997) (2) SCC 302
3 Dalmia Power Ltd vs ACIT (Civil Appeal No 9496-99 of 2019)

Direct tax updates

Cost Inflation Index for Financial Year 2020-21 [Notification No 32/2020 dated June 12, 2020]

Central Board of Direct Taxes has notified cost inflation index for the financial year 2020-21 as 301 (Base date is 1st April, 2001).

New Form 26AS (Annual Information Statement) [Notification No 30/2020 dated May 28, 2020]

A new Section 285BB, introduced by Finance Act 2020 requires the tax department to upload in the registered account of the taxpayer a statement of information relating to taxpayer's specified financial transaction, payment of taxes, demand/ refund and pending / completed proceedings, which is in the possession of an income-tax authority.

Pursuant to above, CBDT has now introduced a new rule 114-I – (Annual Information Statement) and revised Form 26AS with effect from 1st June, 2020 which will now contain information relating to specified financial transactions, payment of taxes, demand/ refund and pending/completed proceedings undertaken by a taxpayer in a particular financial year that has to be mentioned in the income tax returns.

Income Tax Return Forms for AY 2020-21 [Notification No 31/2020 dated May 29, 2020]

The CBDT has notified the Income Tax Return Forms for AY 2020-21. From an overall perspective, the newly notified forms have certain new fields that have been introduced in order to warrant additional information/ disclosures from the taxpayers. Some of the key changes are:

- A new schedule DI has been introduced which seeks details of investments (chapter VIA deductions, deduction u/s 10AA and deductions u/s 54 to 54GB) to be taken into account for determining total income considering the extended deadlines for making such investments;
- Certain additional details are sought from the non-corporate assessees such as details of amount greater than INR 1 crore deposited in a bank account, details of amount spent on foreign travel if amount exceeds INR 2 lakhs, etc;
- An option for opting section 115BAA/ 115BAB (reduced tax for specific domestic companies) is now provided;
- A new Schedule 112A seeking detailed information (such as ISIN Code, name of share/ unit, sale price, full value of consideration, cost of acquisition, FMV as on 31st January 2018, etc) on sale of equity share in a company or unit of equity oriented fund or unit of a business trust
- on which STT is paid under section 112A is introduced.

SEBI REGULATORY UPDATES

JUNE 2020

SEBI Regulatory updates

Informal guidance on rejection of reclassification of promoter's married daughter as public shareholder [1]

The applicant, promoter and managing director of a listed company, desires to gift part of his holding (more than 10%) to his two married daughters ('recipients'). Subsequent to the above transfer, recipients would be classified as promoters of the company. However, since the recipients are not involved in the management of the company and are married and living separate lives, they desire to be reclassified as 'public shareholders' instead of 'promoters'.

SEBI stated that by virtue of definition of 'promoter group' under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, the daughters of promoters are immediate relatives and are a part of promoter group irrespective of the fact that they are married and living a separate life or that they are not involved in management of the company. SEBI also clarified that as per SEBI (Listing Obligation and Disclosure Requirements) Regulations 2015, in case of gift of shares by a promoter/ person belonging to promoter group, immediately on such event, the recipient of such shares will be classified as a promoter/ person belonging to promoter group, as applicable.

Lastly, SEBI has clarified that under Regulation 31A of LODR Regulations, the promoter(s) and/or persons related to the promoter(s) seeking re-classification shall not together hold more than 10% of the total voting rights in the listed entity and therefore, the daughters of promoter would not be eligible to seek re-classification from the promoter group to public.

1 **SEBI/HO/CFD/CMD1/ow/2020 dated June 12, 2020**

SEBI Regulatory updates

SEBI informal guidance : Exempts Proposed Acquirers being private family trust, Karta of HUF and amongst lineal descendants from making open offer under Regulation 11 of the SAST Regulations [1]

SEBI has allowed an application seeking exemption from making open offer under SAST Regulations in the case of proposed transaction of direct acquisition of 12.91% equity shares of the Crimson Metal Engineering Company Limited between the acquirer trust, HUF of promoters and promoters disclosed for a period of less than 3 years (collectively, the acquirers) and transferors being individuals (disclosed promoters for more than 3 years) pursuant to a family arrangement, intended to streamline ownership and welfare of the promoter family.

The matter was placed before the SEBI Takeover Panel ('the Panel') and the Panel recommended grant of exemption as under:

1. In respect of acquisition of shares by the Trusts, the transferors themselves were the trustees and beneficiaries of the Trusts and such transfer would not result in change in control or shareholding of the promoter group and recommended granting exemption;
2. In respect of acquisition of shares by HUFs, the Panel recommended grant of exemption as the shares were proposed to be transferred to the Kartas of HUFs by the respective family members;
3. In respect of transfer of shares between grandchild and grandfather, the Panel recommended granting exemption as the transferor and transferee are lineal descendants.

Considering the recommendations of the SEBI Takeover Panel, SEBI allowed the application thereby exempting the acquirers from making open offer upon acquisition of shares of Crimson Metal Engineering Company Ltd from existing promoters.

[1] **WTM/GM/CFD/10 /2020-21 dated June 5, 2020**

SEBI Regulatory updates

SEBI increases promoters' creeping acquisition limit to 10% under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("Takeover Regulations") [SEBI/LAD-NRO/GN/2020/14, dated June 16, 2020]

SEBI has amended the Takeover Regulations to permit promoters owning 25% or more voting rights in a listed company to increase their stake beyond 5% (creeping acquisition limit) but up to 10% through preferential issue of shares, without triggering the open offer obligation under the Takeover Regulations. The said relaxation is available only for the financial year 2020-21.

SEBI increases promoters' creeping acquisition limit to 10% under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("Takeover Regulations") [SEBI/LAD-NRO/GN/2020/14, dated June 16, 2020]

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SEBI further extends timelines for regulatory filings for AIFs and VCFs [SEBI/HO/IMD/DF6/CIR/P/2020/92 dated June 4, 2020]

SEBI, vide its Circular No. SEBI/HO/IMD/DF1/CIR/P/2020/58 dated March 30, 2020, extended the due date for regulatory filings for AIFs and VCFs for the periods ending March 31, 2020 and April 30, 2020 by two months. SEBI has now provided for a further extension of timelines for regulatory filings for AIFs and VCFs for the months ending March, April, May and June 2020, till August 7, 2020.

RBI REGULATORY UPDATES

JUNE 2020

RBI Regulatory updates

RBI provides relaxation for debt investments by Foreign Portfolio Investors ("FPIs") through Voluntary Retention Route ("VRR") [1]

Currently, FPIs need to invest at least 75% of their 'Committed Portfolio Size' ("CPS") within three months from the date of allotment. In view of the disruptions caused by COVID-19, RBI has decided to allow FPIs that have been allotted investment limits, between January 24, 2020 (the date of reopening of allotment of investment limits) and April 30, 2020, an additional time of three months to invest 75% of their CPS. For FPIs availing the additional time, the retention period for the investments (committed by them at the time of allotment of investment limit) would be reset to commence from the date that the FPI invests 75% of CPS.

CORPORATE LAW UPDATES

JUNE 2020

Corporate Law updates

NCLT approves demerger of investment business from wholly owned subsidiary company into Parent [1]

The said Scheme of Arrangement ("Scheme") was for demerger of investment business from the wholly owned subsidiary i.e. the demerged company by the name of Ensemble Holdings and Finance Limited ("EHFL") to its parent entity or the resulting company being Godrej Industries Limited ("GIL").

The said demerger aimed at achieving the following:

(i) Consolidation of investment of EHFL in GIL; and

(ii) Flexibility to GIL to exit from the NBFC activities of EHFL and to transfer shares of EHFL having NBFC License to another promoter group entity at fair value.

Certain key facets of the Scheme that are noteworthy are that the composition of the undertaking being the NBFC license sitting in the subsidiary along with strategic investment being a very nominal stake (0.60% in this case) in the real estate arm being Godrej Properties Limited.

The said scheme facilitates consolidation of investments of EHFL with GIL, while enabling transfer of shares of EHFL (and therefore, the NBFC license) to the promoter group entity.

Ministry of Corporate Affairs notifies Companies (Share Capital and Debentures) Amendment Rules, 2020 [2]

MCA has amended the Companies (Share Capital and Debentures) Rules, 2014 by allowing companies to issue sweat equity shares not exceeding 50% of its paid-up capital for a period of upto 10 years from the date of its incorporation or registration. Additionally, the requirement with regard to Debenture Redemption Reserve and investment or deposit of sum in respect of debentures maturing during the year is now removed for NBFCs and listed companies issuing privately placed debentures.

1 WTM/GM/CFD/10 /2020-21 dated June 5, 2020

2 Notification dated June 5, 2020

Corporate Law updates

NCLAT dismissed minority shareholders' appeal and upholds NCLT order approving selective capital reduction

Atlas Copco (India) Ltd ("ACIL" or "the Company") was delisted from Bombay and Pune Stock Exchange in 2011. The holding company of ACIL held 96.32% of the share capital and the balance 3.68% was held by non-promoter shareholders. Thereafter, in 2018 the Company filed a company scheme petition before NCLT for selective capital reduction u/s 66 of the Companies Act, 2013 of 3.68% of share capital held by non-promoter shareholders, after passing a special resolution approved by the shareholders. However, a few non-promoter shareholders voted against the resolution and also filed objections to the proposed scheme of capital reduction with NCLT by alleging that offer price as well as proposed capital reduction of 'minority shareholders' is unfair. ACIL submitted an undertaking, on directions of NCLT, that the objecting shareholders can continue as a shareholder. Accordingly, NCLT admitted the application filed by the company for the proposed Capital Reduction.

The objecting shareholders challenged the order of NCLT and appealed before NCLAT. Further, the objecting shareholders reiterated the arguments that the valuation of shares was carried out in an unfair manner and without any due diligence and also stated that the option of retaining shares was not provided at the time of passing special resolution. Also, the objecting shareholder stated that the option of retaining shares through Affidavit filed by company, on direction of NCLT, is unacceptable and the resolution can only be modified by the shareholders in legally convened meeting.

NCLAT upheld NCLT order and dismissed minority shareholders' appeal and held that there was no irregularity in the valuation done by the valuer and accepted the contentions made by the Company that the valuation was undertaken based on past as well as future projections. Further, NCLAT held that the NCLT is imbibed with the powers to modify the scheme and therefore the directions given by the NCLT, pertaining to option of retaining shares by objecting shareholders, is within the four corners of the law.