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The Chamber of Tax Consultants

THE CHAMBER'S JOURNAL

Your Monthly Companion on Tax & Allied Subjects

Vol. XI | No. 3 | December 2022

BUSINESS RESTRUCTURING

GST IMPLICATIONS and Issues

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International Taxation Committee

1st Residential Refresher Conference on the Foreign Exchange Management Act 1999 and its Rules/ Regulations (with focus on practical aspects) held from Friday, 2nd to Sunday, 4th December, 2022 at Hilton Garden Inn, Pune.

Inaugural Session

Seen from L to R: CA Mehul Sheth (Hon. Jt. Secretary), CA Yash Bhatt (Course Coordinator) CA Manoj Shah (Speaker), CA Parag Ved (President), CA Hinesh Doshi (Past President), CA Kirit Dedhia (Chairman), CA Rashmin Sanghvi (Speaker), CA Parag Kotak (Course Coordinator) and CA Dhishat Mehta (Speaker)

CA Parag Ved (President) giving his opening remarks

Seen from L to R : CA Yash Bhatt (Course Coordinator), CA Rashmin Sanghvi (Speaker), CA Kirit Dedhia (Chairman), CA Mehul Sheth (Hon. Jt. Secretary) and CA Parag Kotak (Course Coordinator)

CA Kirit Dedhia (Chairman) welcoming the speakers and delegates.

Seen from L to R: CA Yash Bhatt (Course Coordinator), CA Parag Ved (President), CA Rashmin Sanghvi (Speaker) CA Mehul Sheth (Hon. Jt. Secretary) and CA Parag Kotak (Course Coordinator)

Speakers

CA Rashmin Sanghvi addressing the delegates

CA Paresh P. Shah addressing the delegates

CA Vishal Gada addressing the delegates

Kishore Joshi, *Advocate* addressing the delegates

Moin Ladha, *Advocate* addressing the delegates

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Editorial

Dear Readers,

On the 1st of December, 2022, India assumed the very important role of the Presidency of the "G-20". One of the objectives of this forum is to create an environment for strong, sustainable and balanced economic growth. G-20 has the responsibility to coordinate globally, the economic policies of its member nations, and help arriving at political agreements that are very important in addressing challenges thrown up by global economic interdependence. This is, therefore, a very significant role that India is assuming at a time when the world is experiencing unparalleled multidimensional crises and also when the world is looking at India as the fastest growing and most stable economy. The G-20 forum is also important due to the fact that its members represent more than 80% of the world's GDP, 75% of its International Trade and 60% of the world's population.

Our Prime Minister has stated that "India's G-20 presidency will be inclusive, ambitious, decisive and action oriented." Therefore, the theme of "*Vasudhaiva Kutumbakam*" or "One Earth One Family One Future" is very thoughtful and apt for the current global challenges and what India is aiming at and capable of doing.

Some of the factors which have resulted in the global economic crisis are Covid, which devastated all economies, the Ukraine war, high inflation and soaring interest rates across the world accentuated by Central Banks' Policies to fight inflation. These are some of the major issues which the G-20 will need to address and therefore assuming the G-20 Presidency, at such a critical and crucial juncture, is indeed, a challenging task.

India has identified some of the priority areas which would be discussed and on which action would be taken by the working groups specially formed for this purpose, during its presidency of the G-20 nations. Addressing the issues faced by the world's economy is a continuous and long process but we hope that the G-20, under India's presidency, will be able to successfully, tackle and resolve the issues and challenges which the world is facing and pull it out of the crisis, it is currently going through.

While India is assuming the above important role, the world's population has crossed 8 billion, doubling in 48 years from the 4 billion mark in 1974 and India is slated to become the world's

most populous country next year, surpassing China! As UN projection of population data reflects, and many experts believe, the world's population will not grow forever. The population will peak up for some time and start declining thereafter. Therefore, the key challenge now for India is harnessing the demographic dividend. This refers to the growth in an economy that is the result of a change in the age profile of a country's population. The change in age profile is typically brought out by a decline in fertility and mortality rates. Research indicates that in India, the economic benefit from the demographic transition has been lower than its Asian peers and there is a danger of it tapering further. Moreover, as per the World Bank data, the percentage of women work force in India is much lower than the global average. An appropriate policy framework will have to be put in place for India to be able to encash its demographic dividend.

Despite the challenge of a huge population, our Government continues to take various measures for overall growth of the Country, wellbeing of its countrymen and economic stability. One such measure which the Government had taken six years ago was demonetisation. As per the latest SBI Research Report, currency in circulation (CIC) declined during Diwali week for the first time in 20 years due to surge in digital payments. CIC is now at about 11.8% of GDP. Share of digital transactions rose to 80.4% in 2022 and is expected to reach 88% in F.Y. 2027.

In the latest Monetary Policy RBI raised the interest rates for the fifth time this year. The hike in Repo Rate is 35 basis points, which is very much in line with of the Central Bank's policy to maintain tight monetary conditions since easing of price pressures could give rise to a boomerang of the inflation monster. RBI has also indicated a marginal downward revision in GDP growth. A visible improvement in consumer and business confidence as per RBI surveys is a positive indicator for the future growth outlook.

The current issue of the Journal is on a very important topic, "Business Restructuring - GST Implications and Issues". This subject is of significant importance due to the complex indirect tax issues involved in business restructuring. I would like to place my appreciation for the Journal Committee on record, for thinking of this subject. My sincere gratitude to the authors for sharing their expert knowledge and sparing their valuable time.

Before I conclude, let me share with the readers, a thought for contemplation, in the festive season.

"The greatest obstacle to discovery is not ignorance it is the illusion of Knowledge".

Wish you and your family a Merry Christmas and very Happy and Fulfilling New Year 2023!

VIPUL K. CHOKSI
Editor

From the President

Dear Members,

As we come closure to the end of Calendar year 2022, we have mixed feelings for the year. While there is respite from the Covid and cases are coming down, world witnessed another geopolitical conflict in Ukraine. This has increased energy prices across the globe and there is related inflation. To counter this, Central banks across the globe started increasing interest rates and India is no exception to this. Till now India is able to navigate this troubled waters but it may take couple of years before we land in safe harbor.

At CTC, we just concluded 3 days Residential Refresher Course on the subject of FEMA. It was excellent RRC meticulously planned and executed by our International Tax Committee Chairman, Shri Kirit Dedhia and his team. He and his team deserve pat on the back for this wonderful RRC. We were overjoyed with the response we got from participants and we had to close registration due to capacity constraint of the venue. We had many people in wait list but we could not accommodate them. Similarly, we have closed registration for our GST RRC in January 2023 and Direct Tax RRC in March 2023. There are few slots available on NRRC basis for Direct Tax RRC. Members who could not register earlier, can join on NRRC basis. Henceforth I would request members to register in advance and don't wait till last day.

As I write this message, we have also closed registration for full day workshop on NBFC on 10th December, 2022. We have announced unique virtual program on 20th and 21st January, 2022 on "Nuances of New Age Securities". It is well structured program giving overview of New Age Securities like CCPS, OCRPS, AIF, REIT, InvIT, etc. We will be covering Domestic Tax, International Tax, Accounting, FEMA, Company Law and Valuation of these securities. I am sure members will benefit from this comprehensive coverage of this program. You all are requested to visit website of Chamber to get updated program list.

Recently, CTC has submitted its pre-budget memorandum to Hon. Chairman CBDT and his team. It was interactive meeting with the CBDT Chairman and they have noted down the issues raised by CTC. Lets hope that those suggestions will be taken care in the forthcoming budget. We also had occasion to meet CBDT representatives and share views of the Chamber on the proposed Common Income Tax return. We have conveyed to them that CTC supports new initiatives of the Government and also requested them to implement changes in phase manner.

This months issue focuses on GST implications of Business Restructuring. The issue covers GST implications on Amalgamation, Demerger, Slump sale, Dissolution of firms, Liquidation, etc. I thank all the contributors for their timely articles and I am sure members at large will benefit from their knowledge.

I conclude with best wishes to all the readers.

Jai Hind.

PARAG S. VED
President

CA Dhiren Shah

Business Restructuring – Necessity, Modes and Methods

"Our business is really simple. When a deal and its structure looks like an octopus or spider, just don't do it" - Timothy Sloan (CFO, Wells Fargo)

Timothy has put deal making in very plain and simple words, which may not be a reality in the present world. An attempt should be made to have corporate structures which are plain and simple to the extent possible. Complicated structures, commonly known as Web Structures are quite difficult to understand by various stakeholders and consequently fail to achieve desired objectives. This may also bring in leakages and inefficiencies over a period of time. Accordingly, it is of paramount importance to have a lean and simple corporate structure which ensures smooth implementation, cost efficient fund raising, regulatory compliance, flexibility for repatriation or reinvestment, tax efficiency etc.

Mastering the art of deal making or structuring is not an easy task. One needs to consider implications on all the stakeholders before going ahead with any deal or restructuring exercise. All the stakeholders - be it owners, lenders or regulators - have their own perspectives and requirements. It would be pertinent to critically evaluate the same and match with the objectives which are required to be achieved.

This article summarizes the need / necessity for the restructuring or M&A activities, prevalent modes of restructuring in India and factors, which need thorough evaluation before deciding the final structure for acquisition or business model.

1. Background

Post-Covid 19, Mergers and Acquisitions (**"M&A"**) is a buzzword across the globe. The increase in global M&A activities is mainly to weather the toughest headwinds due to Covid-19, changing geopolitical situation, volatility in commodity prices, high inflation rates etc. Few largest M&A deals globally are –

- Acquisition of Activision Blizzard by Microsoft – USD 68.7 Bn
- Broadcom acquisition of VMWare – USD 61 Bn
- Acquisition of Twitter by Elon Musk – USD 44 Bn

- Oracle acquisition of Cerner – USD 28.3 Bn
- AMD acquisition of Xilinx – USD 28.3 Bn
- Prologis merger with Duke Reality – USD 26 Bn

Similarly, in the last few years, India has also witnessed an exponential increase in M&A activities. India's domestic M&A activity rose over 190 per cent in 2022 to $105.6 billion. The highest share of the total M&A deals was in financial sector services, accounting for $69.4 billion of the total. It saw a whopping 300 per cent jump from 2021. The technology sector saw the highest number of deals totalling $18.6 billion. These deals had a market share of 12.5 per cent[1].

Some of the recent marquee deals in India include –

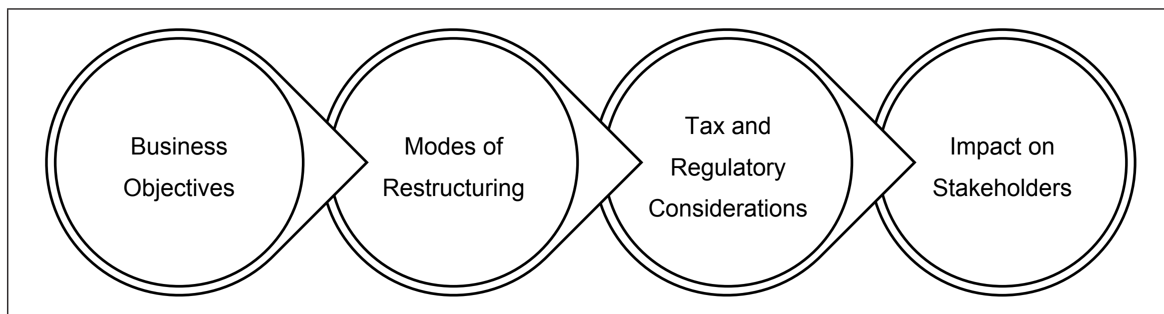
- Merger of HDFC – HDFC Bank
- Merger of L&T Infotech Ltd – Mindtree Ltd
- Merger of PVR-Inox
- Merger of strategic businesses (listed and unlisted companies) with Tata Steel Ltd
- Merger of Zee Entertainments with Sony – largest deal in the sector
- Takeover of Ambuja and ACC by Adani Group from Holcim

The coming year is also expected to be another exciting year in terms of M&A activity, as the investor community has seen certainty in government policies and a liberal regulatory environment. With increasing commitments being made to reduce carbon emissions by companies as a part of ESG initiatives, more funding is likely to be mobilized for the transition to greener sources of energy and thus will create more opportunities for M&A in this space. Other strong reasons for the surge in M&A are the thriving start-up eco-system, availability of global funds, ease of doing business in India campaign (including PLI schemes for various sectors), conducive foreign exchange regulations and most importantly, the global mindset shift in favour of 'China plus one' strategy. Sectors such as infrastructure, renewable energy, healthcare, IT, pharma, e-commerce, banking and financial services are likely to witness a surge in M&A activities in coming years.

2. Life Cycle of Business Restructuring

As stated earlier, business restructuring requires to be in line with the objectives of all the stakeholders and hence it is important to evaluate and understand the objectives to be achieved and critical constraints which need to be overcome while finalizing any deal or restructuring exercise. Typical life cycle of deals/business restructuring is like this —

1. Business standard article titled "M&A activity touches all time high in 2022, 58.2% higher than 2021".



Now let's discuss each component in greater detail.

3. Business Objectives

In this dynamic business environment, undertaking either internal or external restructuring is imperative to increase efficiency and maintain profitability. Corporate restructuring aims to achieve economies of scale, increase market share, cost reduction, risk diversification, reduced competition, improve financial health, geographical diversification etc.

Economies of scale	The merger of two businesses results in various synergies. The merger enables the combined entity to leverage better technology, management expertise, intellectual property rights, backward/forward integration and thus result in significant value creation for the stakeholders. Such economies will occur due to efficient utilization of resources, reduction in competition, optimum use of distribution network, reduction in cost etc.
Increase in Market Share and Reduction in Competition	It is quite common that companies looking for increasing market share generally undertake a horizontal merger/acquisition route, more commonly known as brownfield expansion. In some cases, such restructuring may result in market dominance or lead to a monopolistic situation and could have adverse implications for the public at large. Therefore, it is essential to understand and evaluate regulatory implications such as approval of the Competition Commission of India while envisaging horizontal merger (For example – merger of PVR and Inox, merger of Zee and Sony).
Risk diversification	High-growth conglomerates typically undertake restructuring for the purpose of risk diversification. For example, a company operating in various businesses such as infrastructure, manufacturing, new age businesses (internet-based companies), financial services, etc may house its different businesses into different entities by various modes of restructuring such as demerger, slump sale etc. This could help in ring-fencing the stable businesses (such as manufacturing and infrastructure) from the risks associated with high-growth businesses (such as new-age businesses).

Monetization focus	Demergers/hive-offs are undertaken by various companies with a view to focus on a particular business. Strategically, such identified businesses are grown to gather critical mass and then eventually are listed through IPO or partially divested to private equity investors. Another purpose of such carve-outs could also be to divest non-core assets and focus on core business.
Better financial management	Financial management is at the heart of any business. The right mix of debt and equity generates optimum returns for the investors. For instance, the merger of a business entity having higher debt with an entity having higher owned funds shall result in the right balance of debt and equity. Further, such restructuring exercise will help in improving various financial ratios and thereby increasing fundraising abilities of the combined entity and will result in wealth creation for the shareholders.
Acquisition of strategic asset	In this digital era of technology revolution, it is necessary to keep pace with the latest technology. An existing entity can acquire entities with unique technology to sustain and increase its market share. Further, restructuring of business happens to acquire a certain asset that takes substantial time for its creation (for example construction of power plants) or provides ready infrastructure. It is very common for large corporates to acquire businesses to access their unique technology or business model (acquisition of Netmeds by Reliance Retail or acquisition of Bigbasket by TATA group).
Geographical diversification	Company typically acquires businesses operating in different geography to increase its market share and geographical presence. Cross-border acquisition helps Indian company in entering the foreign market without involving in various regulatory approvals and helps in accessing the ready infrastructure of the foreign entity. This eventually leads to significant synergies and could pave the way for the smooth entry of other brands of the company in the foreign market.

Key takeaway –

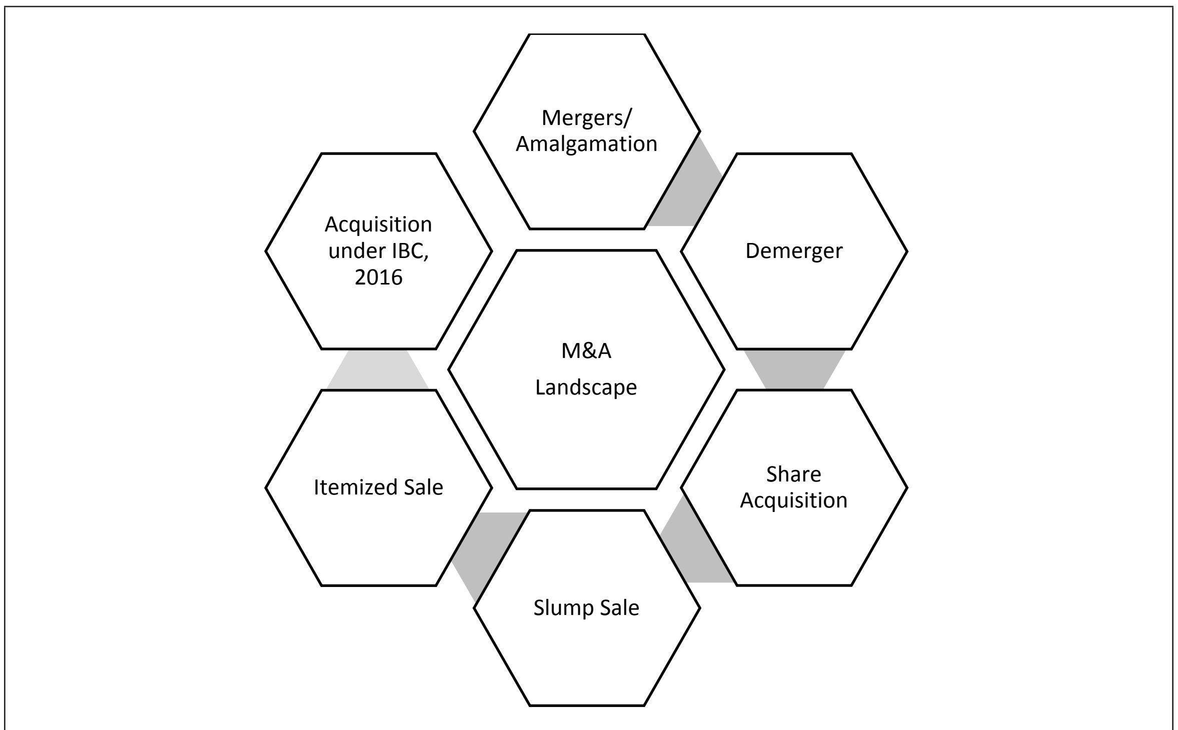
Understanding of what you want to achieve is quite critical before undertaking any M&A or business restructuring exercise. It is advisable to document detailed commercial rationale establishing the need to undertake this exercise. Benefits to all the stakeholders are required to be demonstrated along with critical assumptions to achieve the same. Without strong business objective, the whole exercise may become futile and lead to catastrophic consequences.

4. Modes of restructuring in India

Restructuring activities can be broadly bifurcated into four buckets –

- M&A activities ie actual business acquisition or divestments;
- Corporate restructuring ie consolidation or hiving off of certain business activities;
- Capital restructuring ie reorganization of capital and debt structure of the group; and
- Business Model restructuring ie rearrangement of business models in line with the supply chain strategies adopted

Let's first discuss certain modes for the **M&A activities as well as corporate restructuring:**



4.1 Mergers/Amalgamation

A merger is a combination of two or more entities into one entity. In other words, the merger results in the consolidation of assets and liabilities of the distinct entities into one legal entity. In India, the merger is undertaken through the National Company Law Tribunal (NCLT) process whereby all the assets and liabilities along with employees, contracts, licenses etc. of the transferor company stand transferred to the transferee company. Pursuant to a merger, the shareholders of amalgamating company become shareholders of the amalgamated company. The merging entities cease to be in existence and are merged into a single surviving entity.

Generally, the process of merger through the NCLT scheme is time-consuming and

encompasses multiple stakeholders and regulators such as shareholders, creditors, SEBI and stock exchanges (in case of listed companies), RBI (whereever applicable), Registrar of Companies, Regional Director, etc. In order to expedite the process, the Companies Act, 2013 introduced fast-track mergers for a certain class of companies which seeks to eliminate NCLT from the process. Such provisions are applicable for the merger of small companies and the merger of a wholly-owned subsidiary with the holding company.

Mergers can be Horizontal Mergers, Vertical Mergers or Conglomerate Mergers depending on the facts of each case and the need of the businesses and the objectives which are required to be achieved.

Horizontal Mergers - Horizontal merger is a merger of two companies operating in a similar line of business. Such a merger shall result in market dominance and elimination of competition.

Vertical Mergers - Vertical mergers can be further divided into two parts. Mergers aiming forward integration of business and mergers aiming backward integration of business. Vertical merger in the nature of forward integration means the merger of the supplier entity with the customer entity whereas vertical merger in the nature of backward integration refers to the merger of the customer entity with the supplier entity.

Conglomerate Mergers - A conglomerate merger refers to the merger of two or more unrelated entities. Such merger generally happens for diversification, leveraging unique technology and enlargement of financial resources.

From a tax perspective, the Income-tax Act, 1961 (**"the Act"**) provides[2] for specific tax exemption to the amalgamating company, amalgamated company and the shareholders, subject to satisfaction of certain conditions. Further, the transfer of assets pursuant to the merger does not attract GST.

4.2 Demerger

Unlike amalgamation, in a demerger, the identified business undertaking is transferred from the transferor company to the transferee company and the transferor company continues to remain in existence to carry on other businesses.

Like amalgamation, the demerger also involves the process of NCLT whereby identified assets and liabilities constituting a business undertaking are transferred from the demerged company to the resultant company on a going concern basis. The process of demerger involves the approval of shareholders, creditors and other regulators. Fast-track provisions are also available for demergers. Pursuant to the demerger, the shareholders of the demerged company receive shares of the resultant company.

From a tax perspective, the Act provides[3] for specific tax exemption to the demerged company, resulting company and the shareholders, subject to satisfaction of certain conditions. Further, the transfer of a business undertaking on a going concern basis does not attract GST.

4.3 Share acquisition

Share acquisition is one of the most common modes of acquisition of a business. In a share acquisition, the acquirer purchases

2. Section 2(1B) of the Act.
3. Section 2(19AA) of the Act.

shares/securities of the target entity from the selling shareholders/security holders. The consideration can be in the form of cash or kind.

Unlike merger and demerger, the share acquisition does not involve the NCLT process and therefore, is a preferred mode of acquisition of business where time is of the essence. Typically, all the negotiated terms and conditions between the buyers and sellers are captured in the Share Purchase Agreement ("SPA"). A standard SPA entails the inclusion of critical clauses such as consideration, payment terms, conditions precedent (requisite regulatory approvals, valuation reports, NOCs from income-tax and GST departments, etc), conditions subsequent, indemnities, warranties, etc.

It is common for a buyer to undertake extensive financial, legal, regulatory and tax due diligence before a share acquisition transaction. The share acquisition is not preferred in cases where due diligence exercise findings reveal complex legacy issues or significant litigations involving contingent liabilities. In some of these cases, the parties often consider special arrangements such as hold back mechanism (i.e. deferral of consideration until happening or non-happening of a particular event), indemnities or even consideration adjustment.

4.4 Asset Acquisition

An asset acquisition can be broadly divided into following two parts:

I. Slump Sale

II. Itemized Sale

I. Slump Sale

Like demerger, the slump sale involves the transfer of business undertaking from the transferor company to the transferee company on a going concern basis. However, in case of slump sale, the consideration for transfer of an undertaking is received by the transferor company and not by the shareholders of the transferor company. The consideration can be paid in cash or by the issue of shares by the buyer (which is typically known as slump exchange).

The tax consequences are also different in case of slump sale and demerger. Generally, the demerger is tax neutral and therefore the cost of asset in the hands of the transferor company becomes the cost of acquisition in the hands of the transferee company, whereas a slump sale is a taxable event in the hands of the transferor and consequently the transferee company is also eligible for a cost step up in case of assets for the purpose of claiming the tax depreciation. The transfer of business on a going concern basis is exempt under GST law and therefore, the slump sale of business undertaking does not attract GST.

Given the tax advantages available for slump sale, the tax authorities have been known to challenge the transaction of slump sale, especially in cases where some of the assets or liabilities are retained by the seller (e.g. valuable immovable property). The argument of the tax authorities is that the partial exclusion of assets/ liabilities jeopardizes the concept of the business undertaking and hence, the sale should not constitute a slump sale. There is a plethora of judicial precedents where the courts have held that cherry-picking assets and liabilities should not jeopardize the slump sale, provided such a combination of assets and liabilities constitutes a business activity. Although the controversy looks well settled with multiple favourable

judicial precedents, whether the assets and liabilities being transferred constitute a business undertaking remains a fact-based exercise and hence, every transaction of slump sale should be critically evaluated to obtain comfort on the tax positions.

II. Itemized Sale

In an itemized sale, the acquirer only acquires identified assets from the seller of the asset at an agreed consideration. Like slump sale, the consideration can be in cash or kind. Such itemized sale of assets generally does not constitute the transfer of a business on a going concern basis and hence, the GST exemption is not available for itemized sale. Itemized sale of assets is preferred where the buyer only wishes to acquire selected assets without assuming any liabilities pertaining to such business undertaking.

4.5 Acquisition of business under IBC

In order to revive stressed businesses, the government has consolidated various laws relating to corporate insolvency into 'The Insolvency and Bankruptcy Code, 2016' ("Code"). The objective of the code is to maximize the value of assets of a person under insolvency in a time-bound manner.

In brief, the process of acquisition of business under IBC involves corporate insolvency and resolution process ("CIRP"). Under CIRP proceedings, the resolution applicant (the acquirer of business) gives its resolution plan outlining its financial proposal for various stakeholders of the corporate debtor (the target company). The Committee of Creditors ("COC") evaluates the resolution plan submitted by various resolution applicants and approves the resolution plan giving maximum benefit to the creditors as per the provisions of the Code. Such approval is subject to NCLT approval.

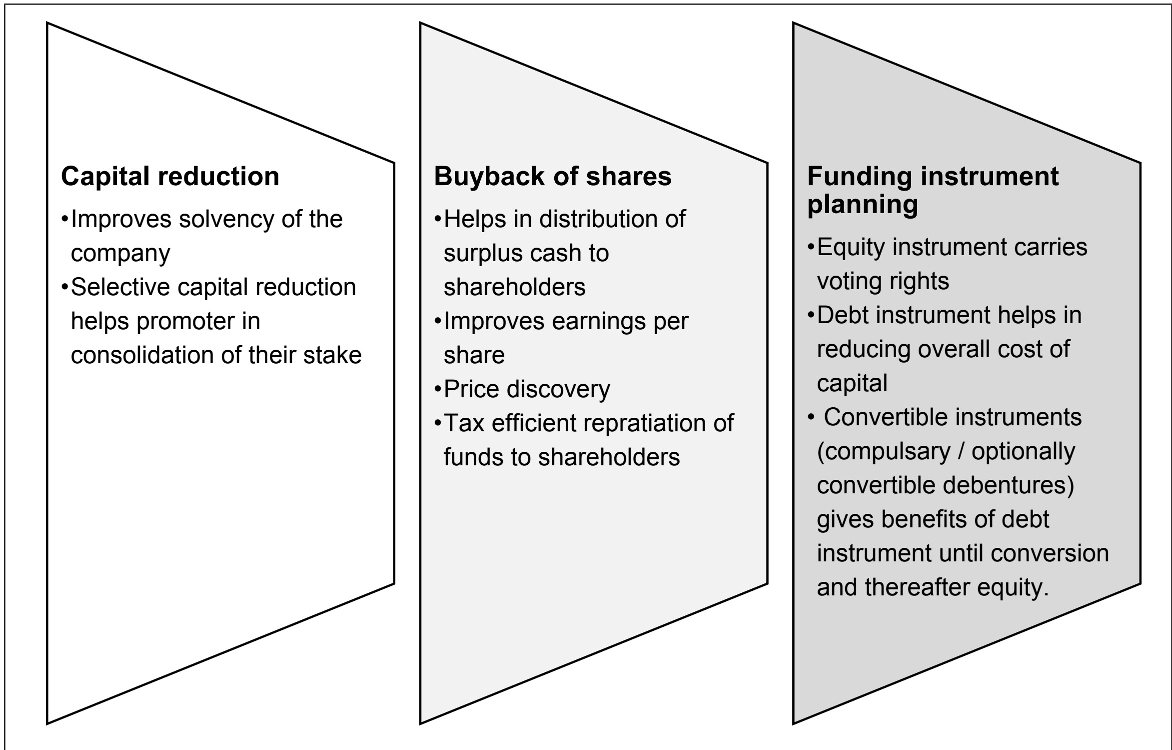
It is obvious that the business under CIRP will have significant liabilities (including tax and other statutory liabilities) as well as contingent liabilities. The provisions of IBC give substantial relief to the resolution applicant with respect to past liabilities or future liabilities in respect of the past period.

While acquiring companies under IBC, the need for restructuring arises with respect to carving out existing and potential liabilities, the exit of existing shareholders, treatment of various stakeholders (financial creditors, operational creditors, government dues etc.) including structuring of the significant debt haircut.

In recent times, various companies are revived due to a change of management pursuant to CIRP proceedings under IBC. For example - acquisition of DHFL by Piramal Group, acquisition of Bhushan Steel by Tata Steel, acquisition of Ruchi Soya by Patanjali, etc. The IBC law is still at a nascent stage and is on a path of evolution with many corporates seeking this route of revival, especially post covid.

5 Capital Restructuring

Capital restructuring plays a pivotal role in the financial health of any organization. Such restructuring helps businesses in optimizing earnings per share, managing tax outflow and improving financial ratios. Capital reduction, buyback of shares, fundraising instruments are some of the common tools for capital restructuring.



6 Restructuring of Business Model

Business model is an essential element for every organization. It is a blend of activities which decides the fate of the business. Business model evolves over a period of time in response to changing internal and external factors. Historically, businesses are valued on the basis of cash flows and profitability. With the changing times, the valuation of a business depends on nuances of business models such as key drivers of revenue, analysis of customer behaviour, cost analysis, market trends, subscriber base, data volume etc. Business models which are in vogue are –

- Full-fledged manufacturer/service providers
- Contract manufacturing / Consignment manufacturing / Low-Risk Distributor
- Asset-light company/asset-heavy company

The decision of the appropriate business model are derivative of different factors including but not limited to –

✓ Nature of industry

✓ Supply chain constraints

✓ Brands / Technology availability

✓ Ringfencing of various risks

✓ Financing constraints/opportunities

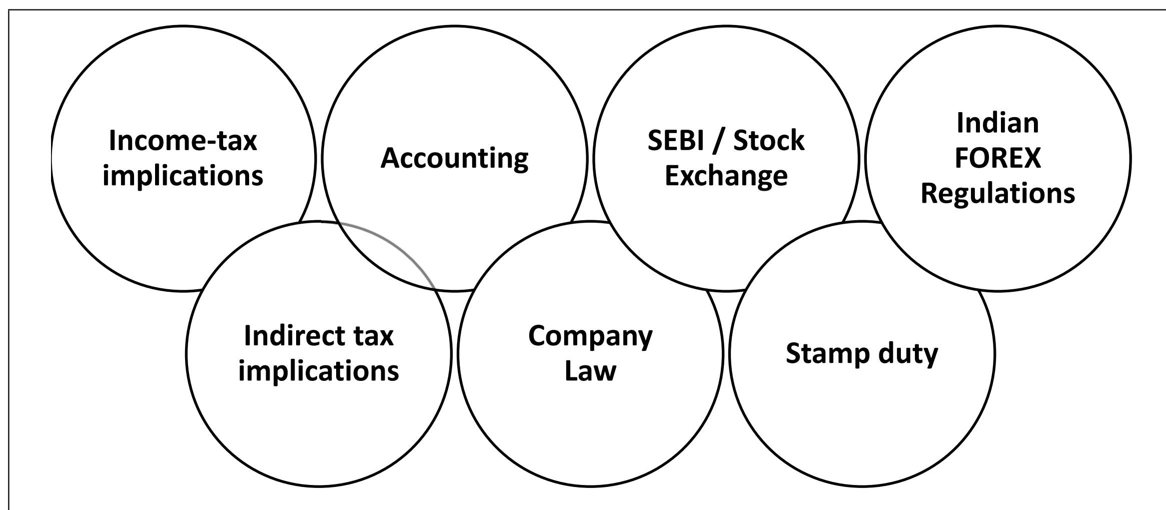
Key takeaway –

As discussed above, there are different options available for executing the M&A or restructuring strategies. As we know, one size does not fit all and hence different alternatives need to be explored while implementing the chosen strategy. Pros and cons of all the possible alternatives are required to be critically evaluated before taking any decision. It is advisable to spend more time and cost beforehand, rather than making any erroneous decision, because unwinding of any structure will also involve substantial cost and management time.

At the cost of repetition, emphasis should be on identification of simple structure which is easy to understand and smooth to implement. Complex structures, though look elegant, could prove to be detrimental in the long run.

7. Key Tax and Regulatory Consideration to be evaluated for restructuring

A 360° review of various tax and regulatory aspects are imperative in any M&A activity. Notably, the following are the key areas which need to be critically evaluated while deciding the mode of acquisition / structuring the business and smooth implementation of the identified option -



Income tax implications	o Tax neutrality/implications in the hands of the transferee and transferor and their owners/shareholders o Implications on carry forward of tax losses and unabsorbed depreciation o Deemed tax implications u/s 56 of the Act in the hands of the transferee

	o No objection certificate from the Income-tax Authority u/s 281 of the Act o Withholding tax implications, especially in case of cross-border transactions o Taxability of write-off / write-back (if any) including implications under MAT in IBC acquisitions o Implications on tax holiday benefits, if any.
Indirect tax implications	o GST applicability on transfer- whether transfer of business constitutes 'transfer on a going concern' basis o Impact on unutilized tax credits o Reversal of tax credits, if required o Implications under foreign trade policies o Implications under various state incentives schemes
Accounting	o Fair value accounting vs. book value accounting under Ind AS 103 o Impact on the net-worth of the company o Impact on various financial ratios o Impact on consolidated accounts, if any
Company Law	o Shareholders/Board/Committee approvals o Implications of related party transactions in case of group restructuring o Corporate law compliances
SEBI/Stock exchange	o Implications of LODR regulations and requirement of open offer o Prior approvals of SEBI/Stock exchanges
Stamp duty	o Specific entry for direct transfer of asset vis a vis transfer pursuant to a scheme of arrangement o Monetary cap on stamp duty in certain states o Applicability of stamp duty in each state, if assets are situated in more than one state

Indian Foreign Exchange Regulations	o Valuation norms to be followed o Fulfilment of FDI sectoral caps and conditions if any o Post-implementation compliances
Regulatory and approvals	o Approvals from respective regulators o Prior approval of CCI, wherever required o Lender's approvals
Timelines and processes	o Time required for the NCLT process o BTA v NCLT process

Key takeaway –

Sometimes tax and regulatory implications can make or break the deal. Detailed due diligence on all the factors is a key step before closing on any deal / restructuring exercise. There are certain instances wherein due to non-availability of regulatory approvals, deals have been put off. Lenders also play a vital role while implementing the structure. In case of NCLT processes, approvals or NOC from all the regulators are necessary and hence, beforehand clarity on each of the above factors are desirable.

Thus, advance evaluation of tax and regulatory implications is necessary to optimize on time and cost (tax and other transaction costs) and avoid any surprises at later stage.

Concluding thoughts

In the current era marred by geopolitical tensions, skyrocketing inflation across the globe, rising global interest rates and consequent looming recession, India offers a silver lining of hope led by political stability, structural reforms, the revival of the capex cycle and domestic consumption. The slowing western economies and struggling Chinese economy could pave the way for fresh foreign investments in India and lead to unprecedented M&A activities in both quantum and scale. The overall buoyance towards India firms up the belief that India is well on course to overtake China and become one of the fastest-growing economies in the world. It is time for the rest of the world to join the bandwagon and be a part of 'India story'.

It is pertinent to close with the quote of Punit Renjen, CEO of Deloitte Global which summarizes the need for precaution before any M&A or restructuring -

"For acquiring companies, the excitement is almost always about where they are going - that is, their strategy for gaining greater growth and productivity. But when mergers fail, it's often because no one focused on who they are - that is, their culture, which is critical to successfully bringing different groups of people together".

CA Naresh Sheth CA Sidharth Sheth

Sale of Business as Slump Sale vis a vis itemised sale - GST Implications

Preamble

The business restructuring is a buzz word in competitive commercial world. Business restructuring helps business entity to realign its operations to maximize its growth and to multiply the returns for promoters or stake holders. One of quite common forms of business restructuring is sale of business, transfer of product line, service line, division or unit to other entity. Such arrangement is made with an intention to create win-win situation for both the entities i.e. transferor as well as acquirer. There is always a dilemma whether to go by slump sale route or by itemized sale of business assets. This decision needs to be taken after considering tax implications (both direct as well as indirect taxes) for both the parties to the transaction. An attempt is made in this article to analyse GST implications of transfer of business as a going concern (slump sale) versus itemized sale of business assets.

A. SALE OF BUSINESS AS SLUMP SALE:

Whether sale or transfer of business is a supply leviable to GST?

Section 7 of CGST Act lays down the scope of supply to include all forms of supply of goods or services or both such as sale, transfer, barter, exchange, licence, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business.

Following are pre-requisites for a transaction to be a 'supply' under GST legislation:

- Transaction should be in relation to 'goods' or 'services';
- Transaction should be of sale, transfer, barter, exchange, lease, rental, license or disposal of goods or services;
- Transaction should be for a consideration (whether or not in money);
- Transaction should be in the course or furtherance of business of supplier.

GST is a levy on supply of goods and/or services. If subject matter of supply is goods or provision of the service, it is leviable to GST. Hence, it is necessary to analyse whether business is 'goods' or 'services'.

Whether 'business' is 'goods' or 'service'?

Term 'goods' is defined u/s 2(52) of CGST Act to mean every movable property other than money and securities. It was matter of heavy debate among professionals whether business is 'goods' for the purpose of GST. One can refer to judicial precedents under VAT law on the same issue. **Hon'ble Allahabad High Court**

in case of *Sri Ram Sahai vs. Commissioner of Sales Tax [(1963) 14 STC 275 (All)]* held that 'business' is admittedly not a movable property and, is therefore, not goods.

'services' is defined u/s 2(102) of CGST Act to mean anything other than goods, money and securities. If one goes by literal interpretation of 'services' definition, 'business' is 'service'.

Transfer of business is categorized as service in the exemption Notification No. 12/2017– Central Tax (Rate) dt. 28.06.2017.

CBIC in its Education Guide issued under erstwhile service tax regime had clarified at para 7.11.15 as under:

"Transfer of a going concern means transfer of a running business which is capable of being carried on by the purchaser as an independent business but shall not cover mere or predominant transfer of an activity comprising a service. Such sale of business as a whole will comprise comprehensive sale of immovable property, goods and transfer of unexecuted orders, employees, goodwill etc. Since the transfer in title is not merely a transfer in title of either the immovable property or goods or even both it may amount to service and has thus been exempted".

Sale/transfer of business or an undertaking for a consideration (in the form of money, shares of acquiring company or any other valuable consideration) is a supply of service when it is done in the course or furtherance of business of transferor.

Whether 'transfer of business' is an activity 'in the course or furtherance of business'?

The transaction or activity done in the course or furtherance of business is a 'supply'. Hence, it is important to deliberate whether sale or transfer of the business can be regarded as an activity carried out in course or furtherance of business.

Hon'ble High Courts in following Sales Tax/ VAT cases held that 'transfer of business' cannot be said to be in the course of business as the business of the dealer is not to sale the business:

- ***Coromandal Fertilisers Limited vs. State of A.P. [1999 112 STC 1 AP HC]*** – Hon'ble Andhra Pradesh High Court
- ***Deputy Commissioner (C.T.), Coimbatore vs. Behanan Thomas [1977 39 STC 325 Mad HC]*** – Hon'ble Madras High Court

Erstwhile Sales Tax/VAT laws did not make specific inclusion of 'transfer of business' in the definition of the term 'business'. Whereas under GST law, term 'business' is defined u/s 2(17)(d) of CGST Act to include ***'supply or acquisition of goods including capital goods and services in connection with commencement or closure of Business'***. One view is that the assessee is closing his business and is transferring the same to transferee. Since such activity is in relation to ***'closure of business'***, same is considered to be 'business' as defined under GST legislation. In view of this, above referred judicial precedents under erstwhile Sales Tax/VAT laws will not hold ground under GST and transfer of business will be treated as supply.

There exists another view that transferee has not closed the business but same is transferred. It, therefore, does not fall under definition of business and hence not a supply leviable to GST. This proposition was accepted by Andhra Pradesh Advance Ruling Authority in case of ***M/s. Shilpa Medicare Limited [2020(39) GSTL 334 (AAR-GST-AP)]*** but it held that transfer of business is a supply. Following are the important observations of Advance Ruling Authority:

- Activity of the 'transfer' is made for a consideration, but neither in the course

of the business nor for the furtherance of the business;

- A going concern is a onetime affair made where the business is sold including assets in entirety or an independent part thereof. Even though this transaction does not amount to a 'supply' as per definition but qualified to be one under the scope of supply as it is backed by the term 'includes' in Section 7(1) of the CGST Act, 2017. Thus, in the broadened interpretation of the term 'includes', this activity is brought under the scope of supply;
- From a plain reading of entry 4(c) of Schedule II to CGST Act it is inferred that transfer of business in entirety along with capital assets does not amount to transfer of goods;
- 'Services' is defined under GST to mean anything other than goods;
- Hence, transfer of business in entirety amount to supply of service and hence eligible for exemption under entry 2 of exemption notification;

Going by this advance ruling, it appears that GST authorities will treat transfer of business as a supply of services leviable to GST.

In this particular case, research and development division of applicant registered in the state of Andhra Pradesh was shifted to Karnataka unit of the said applicant. The above referred advance ruling was overturned by Appellate Authority of Advance Ruling (Andhra Pradesh) on the ground that transfer of business among distinct persons amounts to supply of goods under Clause 4(c) of Schedule II to CGST Act as it is not a transfer of business as a going concern to another person. Here the stress is given that transferee division/unit is not 'another person' as stipulated under clause 4(c)(i) of Schedule II to CGST Act. It may be noted that appellate authority has not rebutted the reasonings and findings of AAR. It has annulled the ruling of AAR on some different ground which was never formed the part of original advance ruling.

The advance ruling (including order of Appellate advance ruling authority) does not have any binding precedence value but it has persuasive value. The decision of appellate advance ruling authority is relevant where the transfer of business is taking place between two different registrations of same entity. One have to take cognizance of this ruling while evaluating GST implications of transfer of business among two distinct persons.

In light of above discussion, the better view seems to treat transfer of business as 'supply of service'. GST legislation provides specific exemption in respect of transfer of going concern. Even if transfer of business is treated as supply, the same would be exempt from GST.

Exemption in respect of transfer of a going concern

Entry 2 of Notification No. 12/2017-Central Tax (Rate) dated 28.06.2017 ('exemption notification') grants an exemption in respect of transfer of going concern which reads as under:

'Services by way of transfer of going concern, as a whole or an independent part thereof'.

Following are the pre-requisites for availing exemption under entry 2 of exemption notification:

- There should be a transfer of entire business/concern (referred as 'undertaking') or an independent part thereof; and

- Such undertaking or an independent part should be transferred on going concern basis.

Following judicial precedents lay down important jurisprudence principle that exemption notification should be construed strictly:

- Hon'ble Supreme Court in case of ***Commissioner of Customs (Import), Mumbai vs. M/s. Dilip Kumar & Co [TS-336-SC-2018-CUST]***;
- Constitution Bench of Hon'ble Supreme Court in case of ***Hansraj Gordhandas vs. H. H. Dave, Assistant Collector of Central excise [1970 AIR 755, 1969 SCR (2) 343];***
- Hon'ble Supreme Court in case of ***Commissioner of Central Excise, New Delhi vs. Hari Chand Shri Gopal [(2011) 1 SCC 236]***

In order to avail exemption under entry 2 of exemption notification, it is incumbent on the transferor to establish that what is transferred is a going concern or independent part thereof. In case of failure to satisfy any of the above pre-requisites, there will be risk of denial of exemption resulting in fastening of GST liability on consideration received on such transfer along with consequential interest and penalty. The department may either treat entire supply as one single supply of business and levy the tax at 18% on entire consideration or treat is as itemized sale and levy GST at rates applicable to individual assets. There are chances that department may treat this as a mixed supply and tax entire consideration at highest rate applicable on any individual asset. For example, if any component of supply is taxable at 28%, entire consideration might be taxed at 28%. It is, therefore, necessary to interpret the phrase *'transfer of going concern, as a whole or an independent part thereof'* properly.

Meaning of the term 'transfer'

Entry 2 of exemption notification exempts **'transfer'** of business as going concern. On plain perusal of the said entry, it may appear that only permanent transfer (i.e. transfer of ownership) of business is exempted from GST.

The word 'transfer' is not defined under GST law. It is settled legal principle that in absence of any definition in the Statue, it must be given same meaning which in ordinary parlance or understood in the sense in which people conversant with the subject matter understand it. This position was upheld by Hon'ble Supreme Court in case of ***M/s. MSCO Pvt. Ltd. [1985 (19) ELT 15 (SC)]***. Ordinarily, when a particular term is not defined in a statute, its dictionary meaning is generally adopted for interpreting the said term.

Dictionary meaning of the term 'transfer' means

- ***To convey from one person****, place or situation to another; move, shift; to cause to pass from one to another;* ***to make over the possession or control of*** *[Merriam-Webster Dictionary]*
- ***To convey****, carry, remover,* ***or send from one person, place or position to another; to make or convey (property, title to property etc.) to another; to make over the possession or control*** *of [Collins Dictionary]*
- *to move someone or something from one place, vehicle, person, or group to another;* ***to make something*** *the legal property* ***of another*** *person; [Cambridge Dictionary]*

From perusal of above dictionary meanings of the term 'transfer', it is evident that 'transfer' includes both temporary transfer (i.e. transfer of possession or control) as well as permanent transfer (i.e. transfer of title).

This view is fortified by Uttar Pradesh Advance Ruling Authority in case of ***M/s. Airports Authority of India [TS(DB)-GST-AAR(UP)-2022-556]*** wherein it was held that *transfer of business for operation, management and development of Lucknow Airport* to M/s. Adani Lucknow International Airport Limited *under the concessionaire agreement for 50 years was held to be transfer of going concern* and hence exempt from GST *vide* entry 2 of exemption notification.

Moreover, scope of supply laid down u/s 7 of CGST Act includes activity of 'sale' as well as 'transfer' within its ambit. However, entry 2 of exemption notification has specifically used the work 'transfer'. Had the intention of legislation to grant exemption only in respect of permanent transfer, they would have used the word 'sale of going concern' instead of 'transfer of going concern'.

The advance ruling does not have any binding precedence value but it has persuasive value.

In light of above discussion, one may take the position that, the word 'transfer' as envisaged under entry 2 of exemption notification includes temporary as well as permanent transfer of going concern. However, possibility of litigation cannot be ruled out.

Meaning of the term 'going concern'

Exemption is available in respect of transfer of going concern or an independent part thereof. It is, therefore, absolutely essential to understand the meaning of term 'going concern'. GST law neither defines the term 'going concern' nor gives any objective parameters to determine what is going concern. GST being a comparatively newer law, lacks judicial precedents on the subject matter.

The transfer of business as a going concern as a whole is known as a slump sale in common parlance.

The term 'Slump Sale' is defined u/s 2(42C) of Income Tax Act, 1961 to mean transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales. This definition is helpful for interpreting the term 'transfer of going concern' used in the exemption notification.

'Going concern' is an accounting concept. SA 570 lists down following prominent indicators as to ascertain whether an entity is a going concern or not:

- Net liability or net current liability position;
- Adverse key financial ratios;
- Indications of financial support by creditors;
- Substantial operating losses;
- Management intentions to liquidate the entity;
- Loss of major market share or major customer;
- Non-compliance with liquidity ratio or other statutory requirements in case of financial institutions.

Above are the good indicators to assess whether an entity is a going concern or not. These are only indicators and not the conclusive parameters though non-fulfilment of such parameters should not be overlooked while assessing whether entity is a going concern. Non-fulfilment of any of the above criteria may not necessarily indicate that entity has violated the going concern assumption.

Erstwhile service tax law also provided exemption for services by way of transfer of going concern. Para 7.11.15 of CBIC Education guide on service tax had clarified meaning of 'transfer of going concern' as under:

"transfer of a running business which is capable of being carried on by the purchaser as an independent business'. Such sale of business as a whole will comprise comprehensive sale of immovable property, goods and transfer of unexecuted orders, employees, goodwill etc."

As per the erstwhile CBEC Education Guide, following are the attributes of transfer of going concern:

- Business which is transferred or proposed to be transferred should be a running business;
- Business should be such which is capable of being run by purchaser as an independent business entity.

It is pertinent to note that what is contemplated under exemption as per erstwhile CBEC education guide was '*transfer of a running business*'. This means that the business which is being transferred by transferor should be an on-going business.

Hon'ble Bombay High Court in case of ***Jayprakash Shamsundar Mandare vs. Laxminarayan Murlidhar Mundade (AIR 1983 Bom 364 AT 367)*** held that:

"if the business is to be characterised as a going concern that business must be run at the time of the assignment. In other words, the business must be a live business, a going business where transaction take place from time to time though not with clockwise regularity. For a business to go on, there must be a stock-in-trade in the premises where that business is carried on…

…One test of determining as to whether the business is a going concern is to find out whether the assignee after the assignment would be in a position to carry on the business which was being carried on in the suit premises by the assignor. If there was a stock-in-trade in the premises, business in would provide which is sought to be transferred, it would provide some indication that there was a business which was a going concern. Ultimately whether a business was a going concern or not is a question of fact."

Internationally accepted guidelines issued by Her Majesty's Revenue and Customs to treat transfer of business as going concern are as under:

- The asset must be sold as a part of a 'business' as a 'going concern';
- Purchaser intends to use the asset to carry on the same kind of business as the seller;
- Where only part of business is sold, it must be capable of separate operation;
- There must not be series of immediately consecutive transfers.

Above referred HRMC guidelines were relied upon by Uttarakhand Advance Ruling Authority in case of ***M/s. Innovative Textiles Limited [TS(DB)-GST-AAR(UTT)-2019-442]*** to rule that Transfer of business as 'going concern' is exempt from GST.

Hon'ble Delhi High Court in case of ***M/s. Indo Rama Textile Limited [2012 (8) TMI 79*** – Delhi High Court] observed as under:

"Upon reading of the aforesaid Section, it is apparent that the definition of Demerger in Act, 1961, would be satisfied if the undertaking that is being demerged is hived off as a going concern, that means, if it constitutes a business activity capable of being run independently for a foreseeable future. To ensure that it is a going concern, the Court while sanctioning a Scheme can certainly examine whether essential and integral assets like plant, machinery and manpower without which it would not be able to run as an independent unit have been transferred to the demerged company."

The term going concern assumes an enterprise to be running for a foreseeable future. This is highly subjective matter and has to be determined on the facts of each case. Following are the examples where it may be difficult to contend that transfer is that of going concern eligible for exemption under entry 2 of exemption notification:

- Transfer of manufacturing unit (along with all assets and liabilities) to builder and developer for constructing commercial premises for sale. The predominant intention of transferee is to carry on real estate business and not to carry on manufacturing activities which was carried by transferor.
- Manufacturing unit which was closed for a considerable period is sold for lumpsum consideration with all its assets and liabilities. In this case, the transferee is not taking over the running business. In fact, there was no business. The substance of the transaction is acquisition of asset and not the acquisition of running business.
- An automobile parts manufacturing unit is transferred to a manufacturer of pharmaceutical products. The transferee intends to commence manufacturing of pharmaceutical products by discarding old machineries, surrendering the existing licenses and taking new licenses for manufacture of pharmaceutical products.

Whether transfer of all assets and liabilities is absolutely necessary for availing exemption under entry 2 of exemption notification?

Another important question arises whether transfer of all the assets and liabilities pertaining to an undertaking is essential to constitute transfer of business as a going concern.

Hon'ble Supreme Court in case of ***Allahabad Bank vs. ARC Holding Limited [2000 (9) TMI 931*** – Supreme Court] held that if the company is sold off as a going concern, then along with the assets of the company, if there are any liabilities relevant to the business or undertaking, the liabilities too are transferred. The said decision was relied upon by Andhra Pradesh Advance Ruling Authority in case of ***SCV Sky Vision [2021 (54) GSTL 339 (AAR-GST-AP)***] wherein it was held that:

"Assessee intending to sell cable network operation business including assets like Set Top Boxes, Local Cable Operators and end-users, except existing and past liabilities, and employees - HELD : Transfer of business was not as "going concern" in context of exclusion of liabilities - Hence "nil" rate of Sl. No. 2 of Notification No. 12/2017-C.T. (Rate) was not applicable."

It is pertinent to note that advance ruling does not have binding precedence. It applies only to the applicant who has sought such ruling.

Hon'ble Delhi High Court in case of ***M/s. Triune Projects Private Limited vs. Deputy Commissioner of Income Tax [ITA 448/2016, CM APPL.26426/2016]*** held that if certain assets or properties are left out because they would cause inconvenience or lead to some kind of a trouble for the purchasing party, it is well within its right to exclude it from the list of assets.

Hon'ble Karnataka High Court in case of ***M/s. Zacharia vs. State of Kerala [1977 (039) STC 0221 Kerala***] held that retention of certain liabilities while transferring the business by the transferor would not devoid the transaction to be categorized as "sale of business" transaction.

Hon'ble Kolkata ITAT in case of ***DCIT vs. Tongani Tea Company Ltd***. observed that even if transfer of specific assets constitutes a 'Going Concern'. It is relevant to analyse whether the business is being transferred along

with all necessary assets and liabilities which are an integral part of the undertaking.

Following judicial precedents wherein it has been held once it is established that the transfer of the undertaking does not obstruct the going concern ability of the undertaking, the non-transfer of select assets/liabilities will not affect the 'going concern' status of the undertaking. Transfer of 'all' assets and liabilities is not mandatory, as long as the business (post transfer of specified assets and liabilities) continues to run efficiently.

- ***DCIT vs. Max India Ltd. [2007] 112 TTJ 726 (Amritsar ITAT);***
- ***Mahindra Engineering & Chemical Products Ltd. vs. ITO (2012) 51 SOT 496 (Mum ITAT)***;
- ***DCIT vs. Mahalasa Gases & Chemicals (P.) Ltd. [2005] 142 TAXMAN 98 (Bangalore ITAT);***
- ***Premier Automobiles vs. ITO [2003] 129 TAXMAN 289 (Bom HC);***
- ***Rohan Software (P.) Ltd. vs. ITO [2008] 115 ITD 302 (Mumbai ITAT);***
- ***DCIT vs. I.C.I (India) Ltd. [2008] 23 SOT 58 (Kolkata ITAT)***

It can be inferred that business assets such as stock-in trade, plant and machinery, un-executed orders and trade liabilities constitute a running business and transfer of such business amounts to transfer of going concern even though some assets and liabilities remain un-transferred provided the transferee is in position to continue the same business without such assets.

Whether exemption under entry 2 of exemption notification can be availed where only division, unit or branch is transferred?

Entry 2 of exemption notification grants exemption in respect of transfer of going concern and also an independent part thereof. A division, unit or a branch constitute an independent part of business and transfer thereof should be eligible for GST exemption under entry 2 of exemption notification.

Under income tax, transfer of business shall be considered as slump sale only when an 'undertaking' is transferred in entirety. Undertaking is defined under income tax Act as under:

"undertaking" shall include ***any part of an undertaking****, or a unit or division of an undertaking or a business activity taken as a whole but* ***does not include individual assets or liabilities or any combination thereof not constituting a business activity****.*

It can be inferred that a business is said to be transferred on slump sale basis even if only a part of undertaking i.e. a unit or division is transferred.

Judiciary, in following cases, held that if a person is carrying on business through different branches, units or divisions which are separately identifiable from each other, transfer of such unit, branch or division having separately identifiable assets, liabilities, income and expenditure would be considered as transfer of business as a 'going concern':

- ***The Deputy Commissioner of Sales Tax (Law) vs. Dat Pathe [1985 (059) STC 0374 Kerala]***
- ***The Deputy Commissioner of Commercial Taxes vs. K. Behanan Thomas [1977 (039) STC 0325 Madras]***
- ***Lohia Machines Limited vs. Commissioner of Sales tax, U.P [1998 (110) STC 0305 – Allahabad]***

Karnataka Advance Ruling Authority in case of ***M/s. Rajashri Foods Private Limited [TS(DB)-GST-AAR(KAR)-2018-172***] held that sell of one fully functional unit including assets

and liabilities attached thereto amounts to transfer of business as going concern and hence exempt from GST.

Uttarakhand Advance Ruling Authority in case of ***M/s. Rajeev Bansal and Sudershan Mittal [TS(DB)-GST-AAR(UTT)-2020-18***] held that transfer of under-construction project under a Business Transfer Agreement is transfer of business as going concern and hence exempt from GST.

Gujarat Advance Ruling Authority in case of ***M/s. Tea Post Private Limited [TS(DB)-GST-AAR(GUJ)-2020-819***] held that transfer of an operation outlet (out of chain of outlets) is not transfer of business as going concern and hence is not eligible for exemption under entry 2 of exemption notification.

Following examples are useful to understand above referred discussion:

- A company having two businesses (i.e. manufacture of steel and cement) transfers cement business to a new company under demerger scheme. Such a transfer of business is eligible for exemption under entry 2 of exemption notification.
- A company having the domestic as well as international business transferring its domestic business (along with all assets and liabilities related to said business) is eligible for exemption under entry 2 of exemption notification.

Whether allocation of consideration for transfer of business to various assets jeopardise eligibility for exemption under entry 2 of exemption notification?

It is common that consideration for transfer of business is determined based on the valuation report wherein values are attributed to major assets. The issue arises whether in such case, GST authorities can deny the exemption on the ground that the transaction is that of itemised sale of assets and not transfer of going concern.

Hon'ble Bombay High Court in case of ***M/s. Premier Automobiles Limited vs. Income Tax Officers and others [(2003) 182 CTR Bom 202***] held that where there is sale of all assets and liabilities of business as a whole for a lump-sum amount, then mere mentioning of value/consideration in respect of land or building will not take the transaction out of Slump Sale Thus where the parties did not intend to make sale of itemized assets, a mere execution of conveyance of immovable property by itself would not constitute sale of itemized assets.

A view can be taken that ascribing value to various assets for justifying valuation of business or for accounting purpose would not jeopardise eligibility for exemption in respect of sale or transfer of going concern.

Transfer of accumulated input tax credit by transferor to the transferee

Section 18(3) of CGST Act read with Rule 41 of CGST Rules entitles transferor to transfer the unutilised ITC in respect of the transferred business undertaking/division/unit to the transferee by filing Form GST ITC-02.

Rule 41 of CGST Rules prescribes the manner of calculating and transferring the accumulated credit to the new undertaking.

In case of demerger of an undertaking, only a part of business in the form of a separate product line, service line, bran, division or unit is sold off as an independent business. In such case, accumulated ITC may belong to the business undertaking as a whole (including the demerged business line). in such cases, proviso to Rule 41 of CGST Rules prescribes that balance of unutilised ITC shall be apportioned in the ratio of value of assets of the new unit. Further, explanation to the said

rule clarifies that value of assets means the value of entire assets of the business whether or not ITC thereon has been availed.

CBIC, vide Circular No. 133 03/2020-GST dated 23.03.2020, clarified certain issues relating to transfer of ITC balance in case of demerger. Summary of such clarifications is as under:

- For the purpose of apportionment of ITC pursuant to a demerger, the value of assets of the new units is to be taken at the State level (at the level of distinct person) and not at the all-India level;
- Transferor is required to file Form ITC-02 only in those States where both transferor and transferee are registered;
- Formula prescribed under proviso to Rule 41(1) of CGST Rules is applicable to all kinds of business re-organizations where only partial business of the undertaking is transferred as a going concern;
- The ratio of value of assets transferred as prescribed under proviso to Rule 41(1) of CGST Rules not to be applied for each head of taxes (i.e. CGST, SGST and IGST). The ratio is to be applied to total balance of all the heads of taxes and cesses (i.e. CGST, SGST, IGST and cess);

  Transferor is at the liberty to determine the amount of ITC to be transferred in each head of taxes subject to the availability of balance in such head (i.e. CGST, SGST, IGST and cess). However, head wise total of ITC to be transferred should not exceed the total ITC amount calculated u/r 41(1) of CGST Rules;
- Apportionment formula for transferring the unutilised ITC to the new unit has to be applied on ITC balance lying in electronic credit ledger as on the date of filing of Form GST ITC-02;
- For the purpose of apportionment of ITC u/r 41(1) of CGST Rules, the ratio of the value of assets should be taken as on the "appointed date of demerger" as specified in the scheme of demerger envisaged u/s 232(6) of Companies Act, 2013.

Issue usually arises as to ITC on goods in transit (as on appointed date) where invoices for such goods are in the name of transferor company. One way of dealing with such situations is to file Form GST-ITC 02 only after availing such ITC in the electronic credit ledger of transferor company.

Hon'ble Delhi CESTAT in case of ***Shree Cement Limited [2002-TIOL-548-CESTAT-DEL]*** and ***Flex Laminator [2002-TIOL-549-CESTAT-DEL]*** held that in case of merger/demerger, credit would be available to the transferee company even if the invoices were in the name of transferor company.

Applicability of above judgements is highly doubtful in GST regime in view of section 16(2)(aa) of CGST Act which provides that a registered person shall be entitled for ITC only if such ITC is appearing in its Form GSTR-2A/2B.

ITC reversal pertaining to exempt supply of 'transfer of going concern' in the hands of transferor entity

Transfer of going concern as a whole or a part thereof is exempt from GST *vide* entry 2 of exemption notification.

Section 17(2) of CGST Act read with Rule 42 of CGST Rules mandates reversal of ITC attributable to exempt supplies.

The department may take the position that common ITC for entire financial year should be reversed in the ratio of value of exempt

supply to value of total supplies (i.e. value of taxable supplies and exempt supplies). The value of transfer of going concern is usually very high. If this method of reversal is followed, practically major portion of common ITC will have to be reversed though a substantial portion of common ITC is incurred for on-going business of the transferor.

Another view on reversal is that section 17(2) of CGST Act applies only when input goods or services are partly used for affecting taxable supplies and partly for affecting exempt supplies. It can be argued that till the date of transfer of business, the entity was engaged exclusively in taxable supply and same position continues even after the transfer of business. As none of the input goods or services are commonly used for affecting taxable and exempt supplies, there is no requirement of reversing common ITC u/s 17(2) of CGST Act read with Rule 42.

Both the above propositions seem to be farfetched. The safer option for transferor would be to reverse the proportionate common ITC availed till the date of transfer of business. As goods or services procured after transfer of business cannot be attributed to exempt supply of 'transfer of going concern', proportionate reversal of such ITC may not be done.

One should take a considered call keeping the facts, stake involved and probable litigation cost in mind on cases to case basis.

B. ITEMIZED SALE OF ASSETS

Under itemized sale of asset, the pre-dominant intention of acquirer is to purchase the assets on pick basis as opposed to acquiring the entire business on as is where is basis. In such a case, transfer of business assets would amount to supply of goods as per Entry 4(a) of Schedule II read with section 7(1A) of CGST Act.

Since GST exemption is available only in respect of services by way of transfer of going concern, itemized sale of asset would be liable to GST at the rate applicable to assets being transferred. If itemized sale of assets consists of transfer of land and/or building, same would not be treated as supply of goods or services (Clause 5 of Schedule III to CGST Act) and consequently not liable to GST.

In case of sale of capital goods, registered person shall pay an amount as determined u/s 18(6) of CGST Act which is higher of the following:

a. Tax payable on transaction value; or

b. ITC to be reversed [as prescribed u/r 44(6) of CGST Rules].

Rule 44(6) of CGST Rules prescribes reversal of ITC equal to ITC involved in remaining useful life (in months) computed on pro-rata basis taking total useful life as five years.

CONCLUSION

The exemption in respect of transfer of going concern is applicable to succession of business, sale of business, amalgamation, merger, demerger and other such forms of business restructuring. One has to be extremely cautious while availing this exemption as risk exposure and stake involved will be huge. There are various issues on which clarity is desired for ease of restructuring the business. The government should clarify such issues through circular or clarification to avoid long drawn litigation.

CA Sunil Gabhawalla

Amalgamation and Merger

1. Introduction

1.1. A 'merger' is generally understood as a combination of two or more entities into one; the desired effect being not just the accumulation of assets and liabilities of the distinct entities, but organization of such entity into one business. It is one of the modes of arrangement entered into between the companies and their members as envisaged under section 230 of the Companies Act, 2013 and is governed by a detailed procedure prescribed under Chapter XV of the Companies Act, 2013, briefly summarised as under:

- Filing of an Application or Scheme with the Tribunal
- Meeting with the creditors & members & Approval by the respective stakeholders
- Sanction of the Scheme by the Tribunal
- Filing of the Tribunal Order with the Registrar

1.2. It is evident that from the perspective of a business, a merger is merely changing the form of corporate ownership and is a transaction in securities between the members of the entities involved. Such change of corporate ownership does not and is not intended to disrupt the continuity of the business operations. In effect the transferee company merely steps into the shoes of the transferor company and takes over all the assets and liabilities including rights under the contracts. This normal rule of law has been confirmed by the Supreme Court in the case of ***CIT vs. Veerabhadra Rao, Koteshwara Rao & Co. 153 ITR 152*** wherein it was held that the successor company shall be eligible to claim bad debts pertaining to debtors taken over from the predecessor company under a scheme of amalgamation.

1.3. As such, an indirect tax law like GST which is concerned with taxation of 'supplies in the course or furtherance of business' should be neutral to such mergers. While the GST law does not contain elaborate provisions dealing with the implications of mergers of two or more entities, the limited set of provisions do revalidate this essence of the neutrality of mergers from GST implications.

2. Legal Provisions

2.1. Section 18(3) of the CGST Act, 2017 provides that where there is a change in the constitution of a registered person on account of sale, merger, demerger, amalgamation, lease or transfer of the business with the specific provisions for transfer of liabilities, the said registered person shall be allowed to transfer the input tax credit which remains unutilised in his electronic credit ledger to such sold, merged, demerged, amalgamated, leased or transferred business in such manner as may be prescribed. It is evident on reading of the said provisions that the GST Law, inter alia, envisages a merger to be mere change in the constitution of a registered person and to align with the fact of continuity of business operations, permits a transfer of the unutilised input tax credit to the transferee company.

2.2. The Supreme Court decision in the case of ***Marshall Sons & Co (India) Limited vs. Income Tax Officer 1997 (223) ITR 809*** held that the date of the merger is the date specified in the Scheme as the "Appointed Date". In view of the prolonged proceedings, it is not uncommon for the said Scheme, which is tentative, to get sanctioned on a date subsequent to the Appointed Date. In view of the above Supreme Court decision, the two companies being merged cease to legally exist from a retrospective date resulting in many consequential substantive and procedural issues and uncertainties. To overcome such challenges, Section 87(2) of the CGST Act, 2017 specifically provides that notwithstanding anything contained in the Tribunal order sanctioning the Scheme, for the purposes of this Act, the said two or more companies shall be treated as distinct companies for the period up to the date of the said order and the registration certificates of the said companies shall be cancelled with effect from the date of the said order. Consequentially, it is also provided vide Section 87(1) that inter se transactions of supply and receipt of goods or services or both shall be included in the turnover of supply or receipt of the respective companies and they shall be liable to pay tax accordingly.

2.3. Section 22(4) requires the transferee company to get itself registered, with effect from the date on which the Registrar of Companies issues a certificate of incorporation giving effect to such order of the High Court or Tribunal.

3. Challenges in Administration

3.1. Having established the essence of the neutrality of mergers from GST implications, it may also be important to recognise that due to a change in the legal owner of the business, there is a need for change in the registration. Most of the rights, privileges and obligations under the GST Law are tied with a particular registration. The GST Law has extensive dependence on online filings, which are pivoted on the GSTIN quoted by various stakeholders. Further, no alternative mechanism of manual filing is provided under the law. This results in many administrative challenges at the ground level.

3.2. This article examines some such practical issues and explains the way forward respecting the legal essence of the arrangement. At a practical level, it is not uncommon for entities to disrupt/re-orient the normal business processes during transition and alleviate some of the pains and litigations. This article does not comment on such disruptions/re-orientations as the outcome of such disruptions/re-orientations could be unpredictable.

3.3. For the purposes of ease of understanding and uniformity, the article considers an example of A Limited getting merged into an existing company B Limited. The date of the Tribunal Order is assumed to be 15.09.2022 and the date when the Registrar gave effect to the said Order is assumed to be 30.09.2022.

4. Registration Related Processes

4.1. As stated earlier, Section 22(4) requires the transferee company to get itself registered, with effect from the date on which the Registrar of Companies issues a certificate of incorporation giving effect to such order of the High Court or Tribunal. However, Section 87(2) deems that the registration of the existing company will be cancelled with effect from the date of the Order of the Tribunal. There is an apparent conflict in the above provisions and if literally read, would result in a period of vacuum between the date of the Tribunal Order and the date of amended certificate of incorporation. On a conservative basis, it may be appropriate for B Limited to apply for registration in each of the States where A Limited was already registered (if B Limited does not already have a registration in the said State) effective from the date of the Tribunal Order. In case B Limited already has a registration in a particular State where A Limited was registered, an application for additional of place of businesses may be required.

4.2. It may also be prudent to prioritise the filings in the case of A Limited and apply for cancellation of the registration in due compliance of the provisions of Section 87(2). In this context, Circular 69/43/2018 permits a liberal interpretation of the timeline for cancellation of registration in case of genuine difficulties.

5. Outward Supplies

5.1. It may be noted that on account of the provisions of Section 87(2), the registration of A Limited will cease to exist on the date of the NCLT Order. As such, it would be prudent to ensure that no tax invoices or other documents are issued in the name and/or GSTIN of A Limited after the said date.

5.2. In case of supplies made prior to the effective date requiring the issuance of credit notes after the effective date, in view of the principles stated earlier, the credit note can be issued by B Limited as a successor of A Limited and reported in his returns accordingly. However, this will result in a mismatch in the customers' records since the invoice would be reflected under the GSTIN of A Limited whereas the credit note would be reflected under the GSTIN of B Limited. This could be

explained at the time of assessment if any query is raised in this regard

5.3. In case of advances received prior to the effective date, the tax would be paid and disclosed by A Limited. However, the invoice would be raised and accounted and disclosed by B Limited. This again can be explained at the time of assessment.

5.4. The largest challenges would arise in the case of claim of refunds on account of zero rated supplies. The entire process of refund on account of export of goods with payment of tax has been automated through the Customs Channel. It would be imperative that the bank account of A Limited be continued till the time the refunds are received. In the alternative, B Limited will have to assert its' rights and entitlement towards the refund as a successor and get the files transferred to the GST Authorities for manual processing. Unluckily no structured instructions have been issued in this regard and therefore the process can be time consuming.

5.5. Similarly, it may be difficult for the taxpayer to explain at the ground level the concept of succession of business through the merger if B Limited files a refund application due to accumulated input tax credit especially if the exports were effected by A Limited. Though there is no legal impediment in this regard, practical experiences can be very different.

6. Input Tax Credit

6.1. In view of continuity of business and the associated timelines, it is possible that an invoice issued by the supplier to A Limited before effective date is received or approved after the effective date and therefore accounted in the books of B Limited. Continuing the principles of neutrality and the decision of the Supreme Court in Veera Bhadra Rao's case (supra), it is evident that B Limited should be eligible for the input tax credit. However, the invoice would be reflecting in GSTR-2B of A Limited and not that of B Limited. Though litigative, it can be argued that as a successor of A Limited, the reflection of credit in GSTR2B of A Limited is a sufficient compliance of Section 16(2)(aa) for the purposes of claiming input tax credit.

6.2. The second proviso to Section 16(2) obliges a recipient to reverse input tax credit if the payment to the vendor is not made within 180 days, with an eligibility of re-credit at the time of actual payment. In the case of a merger, it is possible that a reversal effected by A Limited on account of non payment to vendor would get regularised by means of payment made by B Limited after the merger. Again, on similar principles, B Limited should be eligible to re-claim the credit reversed by A Limited

6.3. The situation can become slightly tricky in case of mismatched credits, where A Limited did not claim the credit because the vendor had not uploaded the invoice in its' GSTR-2B. It is not evident whether post the cancellation of the registration, the vendor would be in a position to upload the credit into GSTR2B of A Limited. Further, it may not be legally correct for the vendor

to upload the credit into GSTR2B of B Limited. In such situations, in view of the principles of substantive compliance, the credit should be available to B Limited based on a certificate issued by the vendor of uploading the credit in the B2C Section due to systems constraints.

7. Transfer of Accumulated Input Tax Credit

7.1. Empowered by the provisions of Section 18(3), the procedural aspects of transfer of input tax credit in case of mergers are prescribed under Rule 41. As per the said rule, a registered person shall, in the event of a merger, furnish the details thereof in FORM GST ITC-02 electronically on the common portal along with a request for transfer of unutilized input tax credit lying in his electronic credit ledger to the transferee. A certificate issued by a practicing chartered accountant or cost accountant certifying that the merger has been done with a specific provision for the transfer of liabilities should also be enclosed. The transferee shall, on the common portal, accept the details so furnished by the transferor and, upon such acceptance, the unutilized credit specified in FORM GST ITC-02 shall be credited to his electronic credit ledger.

7.2. It is apparent that prior to the filing of Form ITC-02, it would be prudent for the transferor to file all the returns till the date of the merger and claim all eligible credits so that the same get reflected in the Form ITC-02. The said filing should ideally present a one time opportunity to transfer the credits from A Limited to B Limited.

8. Transfer of Balance in Electronic Cash Ledger

8.1. There is no provision for transfer of balance lying in electronic cash ledger on account of merger. Therefore, A Limited should file a refund application for the balance lying in the electronic cash ledger. Before applying for the refund, it may be prudent to ensure that all pending TDS/TCS Credits should be accepted so that the same are reflected in the electronic cash ledger.

9. Conclusion

9.1. It is evident that while a merger is expected and intended to be neutral in the context of GST, various procedural issues result in uncertainty and lack of clarity especially in transition cases. It would therefore be useful if the Government can issue a clarification explaining the procedures to be followed in such situations.

"Experience is the only teacher we have We may talk and reason all our lives but we shall not understand a word of truth until we experience it ourselves"

— *Swami Vivekananda*

Abhay Desai
Advocate

Demerger – GST Implications

Introduction

Companies may enter the scheme of arrangement (variation of rights with its shareholders/creditors) for various business reasons. Said event is also known as business reorganization, restructuring or reconstruction. The demerger is one such form. The company may demerge a certain division(s) or product line(s) to an existing company or a new company. It, therefore, alters the rights of the existing shareholders/creditors vis-à-vis the transferor company as they also assume rights in the transferee company. The demerger is undertaken to focus more on the core business as an independent company or to unlock the value of the division(s) by way of a separate listing or separate funding. Whatever may be the objective, for professionals it is imperative to understand the implications that may arise under the GST laws on account of the demerger. In the present paper, we shall first briefly discuss the meaning of the term 'demerger' and then discuss various issues with possible views thereon.

Meaning

The term 'demerger' has not been defined in the GST laws or Company Laws. The general meaning of the said term implies the transfer of an undertaking on a going concern basis by an existing company (referred to as 'demerged company' in the present paper) to a transferee company (existing or newly formed) (referred to as 'resulting company' in the present paper). Income Tax Act, 1961 defines the term 'demerger' u/s 2(19AA) to mean the transfer pursuant to a scheme of arrangement under sections 230 to 232 of the Companies Act, 2013 by a demerged company of its one or more undertakings to any resulting company subject to the stipulated conditions. The key conditions stipulate that all the property as well as liabilities of the undertaking should be transferred on a going concern basis. We can therefore assert that the demerger involves the transfer of an undertaking on a going concern basis.

Demerger process

The following activities are required to be performed to affect a demerger:

- Filing of the Scheme of Arrangement – The scheme of arrangement contains the terms of the demerger. An application along with the stipulated documents is required to be filed before the NCLT seeking an order of conveying a meeting for approving the said scheme.

- Meeting of members/creditors – A meeting is required to be held as per the provisions of the law and the directions of NCLT. The minutes of the meeting are required to be recorded with the facts of the votes cast in favour or against the motion for accepting the scheme. The motion is required to be approved by the majority of the members/creditors provided the vote in person/proxy represents members/creditors holding 3/4th in value of the said total members/creditors.
- Petition and Sanction of the scheme – The chairman of the meeting is to report the result to NCLT. If the scheme is approved in the said meeting, a second petition must be submitted to NCLT seeking approval of the scheme. After hearing the objections, the NCLT will pass an order approving the demerger with or without modifications.
- Filing with the ROC – The NCLT order is required to be filed with ROC within 30 days from the receipt of the same.

One may also appreciate the concept of 'appointed date' and 'effective date'. The appointed date (Sec. 232(6) of the Companies Act, 2013) is the date indicated in the scheme from which the said scheme shall come into force. The effective date (Sec. 232(5)) is the date on which a copy of the NCLT order sanctioning the scheme is filed with the ROC.

With the aforesaid brief context, let us now deal with issues that may arise under the GST laws.

Levy of tax on demerger

An issue may arise as to whether GST can be levied on the transfer of the undertaking by way of the demerger. Sr. No. 2 of Notification No. 12/2017-CT (Rate) dt. 28.06.2017 issued in exercise of powers granted by Sec. 11(1) of the CGST Act, 2017 grants exemption from tax to the services by way of transfer of a going concern, as a whole or an independent part thereof. The term 'going concern' implies a running business (comprising all the assets, liabilities, employees, goodwill, contracts, etc.) which is capable and intended to be run independently by the transferee. It is distinguished from a mere transfer of assets. Further, it may be the entire business which has been transferred or an independent part of the business capable of separate operation. It may also be noted that the said exemption presumes that the transfer of a going concern is a 'service'. It is so because the said transfer does not merely entail a transfer of goods. It can therefore be contended that the transfer of the undertaking by way of the demerger cannot be brought to tax.

One may also consider whether recourse to the aforesaid exemption is actually required in the case of the demerger. This is so because Sec. 9(1) of the CGST Act, 2017 r/w Sec. 7(1)(a) of the said Act provides for the levy of tax on all forms of supply of goods or services or both made for a consideration by a person in the course or furtherance of business. Only if the demerger is found to be covered by the said charging provisions that the recourse to the exemption may be found necessary. The existence of an exemption cannot imply the charge of tax otherwise ***(Associated Cement Companies Ltd vs. State Of Bihar 2004 (7) SCC 642)***. The levy is attracted only to the supply made 'in the course or furtherance of business'. The term 'business' has been defined u/s 2(17)(a)/(b) to include any trade, commerce, etc. and any activity or transaction in connection with or incidental or ancillary

to such trade, commerce, etc. Therefore, the activity leading to the cessation of business *qua* the transferor cannot be said to have been undertaken in the course or furtherance of business. One may also consider that Sec. 2(17)(d) includes the supply or acquisition of goods including capital goods and services in connection with the commencement or closure of business. The same applies *qua* the 'supply' in connection with the closure. Therefore, it cannot apply to the transfer of business itself.

One may also note that Sec. 7(1)(c) read with Sr. No. 1 of Schedule I cannot apply to the situation of a demerger since the said provisions apply to the permanent transfer or disposal of business assets as opposed to the situation of a demerger which entails the transfer of the undertaking as a going concern. On the same ground, one can also say that Sr. No. 4 of Schedule II cannot apply to demerger.

Therefore, it can be contended that since the demerger is not covered by the charging provisions (and hence not a 'supply') recourse to the exemption notification is not warranted.

One may consider the following judicial rulings on the given issue:

- ***Deputy Commissioner vs. K. Behanan Thomas [1977] 39 STC 325 (Mad.)*** – Held that the proceeds from the transfer of business cannot be said to be proceeds made in the course of business. Further, it was held that such proceeds also cannot be said to be in connection with or incidental or ancillary to the business. Hence it was held that the question of claiming exemption under Rule 6(d) (which granted a deduction to the proceeds from the transfer of business) arises only if such proceeds are part of the turnover. Since the proceeds from the sale of the business cannot be part of the turnover, the question of exemption shall not arise. It was also held that it is not necessary that the assessee must entirely go out of business post sale or that such business must have a separate registration. Sale proceeds of a branch which is an independent unit by itself would qualify as a sale of a business.
- ***Zacharia vs. State of Kerala [1977] 39 STC 221 (Ker.)*** – Held that the mere fact that the seller had undertaken to settle liabilities which had accrued prior to the sale of the business would not by itself show that the seller had not transferred the business as a whole. So long as there is nothing to suggest that any part of the assets was retained by the seller or any amounts standing to the credit of the business were taken over by the seller, it cannot be suggested that the business as a whole was not transferred.
- ***Monsanto Chemicals of India (P.) Ltd. vs. State of Tamil Nadu [1982] 51 STC 278 (Mad.)*** – Held that a person may carry on several lines of business and each line of business would be a unit of business by itself.
- ***Coromandal Fertilisers Limited vs. State of A.P. 1998 (6) ALT 730 (AP) (Full Bench on reference)*** – Held that the transfer of an entire business undertaking together with the moveable properties, even if it involves the sale of goods, cannot be regarded as a sale in the course of business by the dealer as the seller intends to put an end to the business.

- ***Paradise Food Court vs. State of Telangana 2017-VIL-238 (AP)*** – Held that even the amendment in the definition of 'business' by including 'any transaction in connection with or incidental or ancillary to the commencement or closure of such trade, commerce, manufacture, adventure or concern' cannot override the ratio of Coromandal Fertilisers supra and hence the transfer of business in entirety cannot come within the charging provisions unless the charging section makes even the transfer of a business as a whole chargeable to tax or if the definition of the word 'sale" does not use the expression 'in the course of trade or business'. Also held that the provisions restricting the input tax credit attributable to the transfer of business reiterate that the transfer of business is not liable to tax. Also held that mentioning all the assets of the business individually with their value in the Schedule cannot lead to the levy of tax as the transaction continues to be of the transfer of a business as a going concern.
- ***Triune Projects Pvt. Ltd vs. DCIT [TS-6237-HC-2016 (Del)]*** – Held in the context of Income Tax that leaving out defunct or superfluous assets of an undertaking will not vitiate slump sale as there is common and commercial sense behind such decisions (the principle should also apply to indirect taxation).

ITC *qua* the demerger

Sec. 16(1) of the CGST Act, 2017 permits the availment of the ITC on the inward supplies used in the course or furtherance of business. On the other hand, Sec. 17(2) of the CGST Act, 2017 restricts ITC attributable to exempt supplies. If the view is entertained that the transfer of business by way of the demerger is not a supply (as it is not in the course or furtherance of business), the ITC related to the said transaction will not be admissible u/s 16(1) as it permits ITC only on supplies used in the course or furtherance of business. If the view is entertained that the transfer of business by way of the demerger is exempt from tax (vide Sr. No. 2 of NN 12/2017-CT (Rate)), then the ITC attributable to the said exempt supply gets restricted u/s 17(2).

Hence it appears that the ITC in respect of the expenditure incurred exclusively on the demerger may not be available. One may however consider the possibility (fact-based) of attributing the given expenditure as common in nature (to facilitate the demerger as well as to facilitate the remaining business qua the transferor outlining the benefit of the demerger on the remaining business) and apply Sec. 17(1) of the CGST Act, 2017 (ITC restricted for non-business) r/w Rule 42(1)(j) for reversing 5% of the common ITC.

Registration

Sec. 22(4) of the CGST Act, 2017 carves a special provision overriding the general provisions in respect of registration to provide that in a case of transfer pursuant to sanction of a scheme or an arrangement for amalgamation or, as the case may be, the demerger of two or more companies pursuant to an order of a High Court, Tribunal or otherwise, the transferee shall be liable to be registered, with effect from the date on which the Registrar of Companies issues a certificate of incorporation giving effect to such order. This is so given the peculiar nature of the transaction that the transfer comes into effect

from the date of filing of the scheme with the ROC. The resulting is therefore required to apply for registration u/s 25(1) within 30 days from such date. Further as per Sec. 85(2) of the CGST Act, 2017 in case of a demerger to a resulting company which is already in existence and registered under GST, an amendment in the registration certificate for including the details of the transferred business will be required.

Transfer of ITC

Sec. 18(3) of the CGST Act, 2017 provides that the registered person shall be allowed to transfer the input tax credits (ITC) which remain unutilized in his electronic credit ledger in the case of demerger amongst other types of transfer. Rule 41 of the CGST Rules, 2017 contains the mechanism for the said transfer. It may be noted that the law does not permit the transfer of the balance available in the electronic cash ledger. This as such should not pose an issue since the demerged entity can always claim a refund of the excess cash balance.

Now the first issue is whether it is mandatory for the demerged company to transfer the ITC if the balance is available. Sec. 18(3) uses the expression 'should be allowed to transfer'. Rule 41(1) also provides that the registered person shall furnish the stipulated details on the GSTN portal in FORM GST ITC-02 along with a request for transfer. Hence it can be contended that it shall not be mandatory for the demerged company to seek a transfer. However, if the transfer is envisaged, the same shall be undertaken as per the mechanism prescribed in Rule 41.

The next issue relates to the way the transferable ITC is determined. Proviso to Rule 41(1) provides that in the case of a demerger the ITC balance shall be apportioned in the ratio of the value of assets of the new units as specified in the demerger scheme. CBIC has issued Circular No. 133/03/2020-GST dt. 23-3-2020 clarifying various aspects related to Rule 41 as under (in the context of demerger):

- that the value of assets is to be taken at the State level (at the level of a distinct person) and not at the all-India level.
- that the transferor is required to file FORM GST ITC-02 only in those States where both transferor and transferee are registered.
- that the ratio of the assets shall be applied to the total amount of unutilized ITC and hence is not required to be applied separately in respect of each head of ITC (CGST/SGST/IGST).
- that once the allowable ITC is determined with respect to the total unutilized ITC, the transferor shall be at liberty to determine the amount to be transferred under each tax head (IGST, CGST, SGST/UTGST) within this total amount, subject to the availability of balance in the specific heads. Further, the said formula shall also be applicable for apportionment of Cess between the transferor and transferee.
- that the apportionment formula shall be applied on the ITC balance of the transferor as available in the electronic credit ledger on the date of filing of FORM GST ITC-02 by the transferor.
- that the ratio of the value of assets should be taken as on the "appointed date of the demerger."

There is also a requirement under Rule 41(2) to submit a copy of a certificate issued by

a practising chartered accountant or cost accountant certifying that the demerger has been done with a specific provision for the transfer of liabilities.

An issue may arise in a situation where the demerged company and the resulting company are in different States. The law does not restrict the transfer of the unutilized ITC in such situations however the aforesaid Circular as well as GSTN portal permits the transfer only if both entities are in the same State. This might have been done to avoid the transfer of the SGST balance from one State to another State. However, the said reason does not justify restricting the transfer of balance available under CGST and IGST head. It is a settled law that a Circular cannot override the express provisions of the law. Hence it can be contended that the balance available in CGST/IGST should be allowed to be transferred to the resulting company in another State.

An issue may also arise with respect to the expression "value of assets" used in Rule 41(1). The Explanation clarifies that the "value of assets" means the value of the entire assets of the business, whether or not input tax credit has been availed thereon. Whether the assets that are outside the purview of GST (such as cash/bank balances, investments, receivables, etc.) are also required to be considered for the determination of the transferable ITC? Whether the assets (such as deferred tax, building leases, etc.) which are created only to comply with the requirement of the Accounting Standards are also required to be considered? It may be noted that the question of availment of ITC never arises on such assets as they are not leviable to the tax. The expression 'entire assets' used in the Explanation suggests that the ratio of all the assets between the demerged company and the resulting company is required to be taken irrespective of whether GST is leviable on such assets or not. The expression 'whether or not input tax credit has been availed thereon' can be said to only suggest that availment of ITC shall be an irrelevant factor for the determination of the value of the assets. Hence a view can be taken that even the value of assets outside the ambit of GST is required to be considered for the determination of the transferable ITC.

Availment of ITC post the effective date

Issues may arise as regards the availment of the ITC post the effective date of transfer in respect of the inward supplies which have been received prior to the said date. Illustrative situations can be:

- ***Mismatch with GSTR 2B***

  Sec. 16(2)(aa) of the CGST Act, 2017 r/w Rule 36(4) of the CGST Rules, 2017 restricts the availment of the ITC until the same is reflected in GSTR 2B. A situation may arise wherein the demerged company may not have been able to avail of the ITC in respect of the supplies attributed to the transferred undertaking since it has not been reflected in GSTR 2B before the effective date of transfer. Can the said demerged company still avail of the ITC post the effective date? It can be contended that all the conditions stipulated u/s 16 r/w Rule 36 barring the condition related to reflection in GSTR 2B stood satisfied at the end of the demerged company before the effective date. Further, the law does not deny the ITC to the demerged company in respect of supplies received by it before the effective date on the ground of reflection

of the said otherwise eligible ITC in GSTR 2B after the effective date. Hence a view can be taken that the demerged company can avail of such ITC.

- ***180 days condition***
  A situation may arise wherein the demerged company has reversed the ITC under the second proviso to Sec. 16(2) of the CGST Act, 2017 on account of failure to pay the vendor within a period of 180 days in respect of the supplies related to the transferred business and the outstanding liabilities are now settled by the resulting company as it assumes all the liabilities pertaining to the transferred business. Who shall then be entitled to re-avail the ITC? The third proviso to Sec. 16(2) provides that the recipient shall be entitled to avail of the ITC on payment made by him of the outstanding amount. Sec. 2(93) defines the term 'recipient' to include a person who is liable to pay the consideration. It can therefore be contended that the expression 'payment by him' in the said third proviso should also include the payment by the resulting company after assuming the liabilities with the approval of NCLT as this leads to the satisfaction of the original debt. It can therefore be contended that it is the demerged company who was the recipient at the time of the receipt of the inward supply and hence it is the said company who shall be entitled to re-avail the ITC on payment by the resulting company.

- ***Goods in transit***
  Who shall be entitled to avail of the ITC in respect of goods in transit qua the transferred business? The issue arises since the receipt of the goods does not take place before the effective date. We have already seen earlier that the condition of reflection of ITC in GSTR 2B after the effective date cannot lead to the denial of the ITC to the demerged company. Now an Explanation to Sec. 16(2)(b) provides that it shall be deemed that the registered person has received the goods where the goods are delivered by the supplier to the recipient or any other person on the direction of such registered person whether acting as an agent or otherwise. It can therefore be contended that the goods in question have been delivered to the resulting company on the direction of the demerged company (as it is this company who files the scheme of arrangement). Hence it can be contended that the demerged company is in receipt of the goods that have been delivered to the resulting company and hence shall be eligible to avail of the ITC.

Reversal of the ITC

A situation may arise wherein the demerged company transfers capital goods on which it has availed the entire ITC and subsequently paid the pro-rata ITC (owing to common use for taxable/exempt supplies) for certain months as per Sec. 17(2) of the CGST Act, 2017 r/w Rule 43 of the CGST Rules, 2017. If on the effective date, the period of 60 months (useful life as per Rule 43) has not elapsed, whether the resulting company is liable to pay the amount under Rule 43 for the balance of months? The harmonious reading of clauses (h) and (i) of Rule 43(1) entails that the obligation of subsequent payment

rests only with the person who has claimed the ITC. Hence it can be contended that the resulting company in absence of any claim of ITC cannot be burdened with the obligation under Rule 43. One may consider the ratio of the decision in the case of ***Saraswati Industrial Syndicate vs. CIT (1990) Supp (1) SCR 332 (SC)***. Sec. 41(1) of the Income Tax Act, 1961 deemed as income the remission of trading liability at the hands of the assessee who had claimed the same as expenditure in previous years. In the said context it was held that the given provisions are attracted only if the identity of the assessee in the previous year and subsequent year remains the same and hence it was held that the amalgamated company cannot be made liable to tax on remission of trading liability since the claim of expenditure was made prior to amalgamation by the amalgamating company.

Credit notes and debit notes

An issue may arise as regards which entity can issue tax credit/debit notes post the effective date in respect of supplies made before the said date. Sec. 34(1) of the CGST Act, 2017 permits the registered person who has made the supply to issue the tax credit notes. Similar provisions exist for debit notes. The said provisions, therefore, permit only the registered person who has made the supply to issue the tax credit/debit notes. It may also be noted that the issuance of the tax credit/debit notes only alters the transaction value of the supply already made and does not result in an independent supply. Hence it can be contended that it is only the demerged company which had made the supply before the effective date that can issue the tax credit/debit notes.

Demands and Recovery

Sec. 85(1) of the CGST Act, 2017 provides that in case of the transfer of business in whole or in part, the transferor, as well as the transferee, shall be jointly and severally liable wholly or to the extent of the transfer to pay the tax, interest or any penalty due from the transferor upto the time of transfer irrespective of whether such liability has been determined before the date of transfer and remains unpaid or the liability has been determined thereafter. Since Sec. 85(1) supra covers all forms of transfer (by using the expression 'in any other manner whatsoever'), even the demerger of business which entails the transfer of an undertaking from the demerged company to the resulting company shall be covered within its ambit. It may be noted that in absence of such provisions, the transferee cannot be made liable to pay tax on supplies effected by the transferor (***DCTO vs. Sha Sukhraj Peerajee 1967 SCR (3) 661 (SC)***).

Sec. 85(2) of the CGST Act, 2017 provides that the transferee shall be liable to pay the tax on the supply effected by him with effect from the date of such transfer and the registered shall apply for the amendment of the certificate of registration. We have also seen earlier in the context of coming into existence of a new resulting company that u/s 22(4) of the CGST Act, 2017 the said resulting company shall be liable to register with effect from the date on which the ROC issues a certificate of incorporation.

An issue may arise as to whether the show-cause notice and the adjudication thereof can be undertaken directly against the resulting company in respect of the liability upto the time of transfer. It may be noted that Sec. 85(1) supra fixes joint and several liability

in respect of the tax, interest and penalty 'due' from the transferor (i.e., the demerged company). Further Sec. 73(1) or 74(1) of the CGST Act, 2017 permits the issuance of the SCN on the 'person chargeable with tax' or 'to whom the refund has erroneously been made' or 'who has wrongly availed or utilised input tax credit'. Hence Sec. 85(1) are recovery provisions and the demands for the liabilities upto the time of transfer are required to be determined only against the demerged company. It is only on non-recovery of the same that the recovery can be initiated against the resulting company.

Another issue may arise as regards the liability on the supplies made between the appointed date and the effective date. As stated earlier, although the scheme of arrangement comes into effect from the effective date (ROC filing), the same at times is made applicable from an earlier appointed date. In other words, the benefits, as well as liabilities from the appointed date, stands accrued to the resulting company. Sec. 85(2) of the CGST Act, 2017 provides that the transferee shall be liable to pay the tax from the date of transfer. Sec. 22(4) also provides for modalities for seeking the registration from the effective date. Hence a harmonious construction entails that the resulting company shall be liable to pay the tax on the supplies effected on and after the effective date.

Another issue may arise in a situation wherein a certain time elapses between the effective date and the actual date from which the resulting company can start issuing the tax invoices in its name. This could be due to the time needed to obtain approvals under other laws (post the issuance of the certificate of incorporation by ROC). During the said time span, the resulting company may continue to use the identity of the demerged company for operational purposes. In such a situation, one may consider putting an appropriate clause in the scheme of arrangement providing for the extension of the effective date to complete various compliances with the laws. It can therefore be contended that the approval granted by NCLT to the said scheme is required to be read into Sec. 85(2) of the CGST Act, 2017 to determine the date from such the resulting company shall be liable to pay the tax. One may also refer to the decision in the case of ***L and T Hydrocarbon Engineering Ltd. vs. UOI (SCA No. 11308 of 2019) (Guj.)*** wherein it has been held that demand of the excise duty again from the successor entity on which excise duty had already been deposited by the transferor cannot be sustained. It was also held that the Central excise department is bound by the Order of the High Court approving the scheme of the demerger and that duty paid by the transferor ought to have been adjusted against the duty, if any, payable by the transferee. The Court also observed that this may not be a problem peculiar to the central excise law alone as such disputes can equally arise under the GST laws also.

Conclusion

A perusal of the above discussion indicates that several issues shall arise under GST in the context of the demerger. One is required to understand the same and accordingly guide the trade to ensure compliance. Proper study and care shall certainly add value to the trade and industry.

CA Kartik Solanki

Transfer of Business through Share Acquisition and Partner's Share in LLP/Partnership Firm

Transfer of business through share acquisition

A. Introduction

- In Mergers & Acquisitions, the mode of acquisition is a crucial factor since the implications may vary on the basis of the structure of mode of acquisition (such as merger, demerger, slump sale, purchase of equity shares etc). Different structures result in distinct levels of tax costs in a transaction, and the transactions would need to be structured accordingly to address the likelihood of potential tax costs. Also, the timelines to complete the transaction can also depend on the mode of acquisition selected.

- Transfer of business through share acquisition is one of the most common modes of acquisition. In this mode, the acquirer simply acquires the company ('Target entity') which owns and operates the business by purchasing the equity share capital of the Target entity, from its existing shareholders.

- Since in case of transfer of shares, only the ownership of the equity shares is transferred from the seller to the acquirer, and the entity carries on the operations as it is, the issues pertaining to indirect taxes such as transfer of input tax credit ('ITC') or determination of tax liability on transactions between appointed date and effective date etc which arise in other modes of business acquisition (e.g. slump sale, merger, demerger etc) would not arise. The only question which arises is determination of GST liability on sale of shares by the sellers.

- Let us now look at the implications under GST law of the transfer of business by acquisition of the shares.

B. Share Acquisition – Whether supply under the GST law?

- Under the GST laws, GST is leviable on supply of goods (except specified goods such as petroleum products, alcoholic liquor for human consumption, etc.) or services for a consideration. In this regard, it becomes relevant to assess whether the shares are goods or services. For such assessment, let us refer to the definition of the terms 'goods' and 'services' under the Central

Goods & Services Tax Act, 2017 ('CGST Act'), which are reproduced hereunder:

"(52) "goods" means every kind of movable property other than money and securities but includes actionable claim, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before supply or under a contract of supply;"

"(102) "services" means anything other than goods, money and securities but includes activities relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination to another form, currency or denomination for which a separate consideration is charged;"

- It is pertinent to note that the term 'securities' is excluded from the definition of both 'goods' and 'services'. The term 'securities' is defined under Section 2(101) of the CGST Act to have the same meaning as assigned to it under Section 2(h) of the Securities Contract (Regulation) Act, 1956 ('SCRA').
- The term 'securities' is defined in an inclusive manner under Section 2(h) of the SCRA. The relevant extract of the definition is as follows:

"(h) "securities"- include

(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or a pooled investment vehicle or other body corporate;

... "

- In this regard, it now needs to be examined as to whether the shares of a public/private company are covered under the purview of the term 'securities' under the SCRA.

C. Shares of a public company, listed on a Stock Exchange – Whether securities under the SCRA?

- The shares of a public company (which is listed on a Stock Exchange) are capable of being bought and sold on the Stock Exchange. Consequently, the same would satisfy the aspect of 'marketability' prescribed under Section 2(h)(i) of the SCRA. Hence, shares of a public company, listed on a Stock Exchange would be treated as 'securities' under Section 2(h) of the SCRA.

D. Shares of an unlisted public company – Whether securities under the SCRA?

- There have been multiple disputes as to the applicability of the provisions of the SCRA qua the shares of an unlisted public company. However, it is relevant to refer to the Supreme Court judgment in case of

Bhagwati Developers Pvt. Ltd. vs. Peerless General Finance & Investment Company and Anr. [2013 (7) TMI 606 – SC] where the Supreme Court had held that whatever is capable of being bought and sold in a market is 'marketable' and there is no warrant to restrict the interpretation of the term 'marketable securities' to include only those securities which are listed on a Stock Exchange. Consequently, shares of a public unlisted company would also be covered within the ambit of the term 'securities' under the SCRA.

- With this judgment, the issue seems to be settled as far as unlisted public companies are concerned. Accordingly, the shares of unlisted public companies would be treated as being 'marketable', and hence, the same would be covered within the ambit of the term 'securities' under Section 2(h) of the SCRA. Consequently, no GST would be applicable on sale of shares of unlisted public companies.

E. Shares of private company – Whether securities under the SCRA?

- As regards the shares of private companies, the Bombay High Court in ***Dahiben Umedbhai Patel vs. Norman James Hamilton [1982 (12) TMI 149 (Bom.)***] had held that since the securities of a private company do not possess the 'character of liquidity' and are not 'marketable securities' as per the definition of 'securities' contained in Section 2(h)(i) of the SCRA, it may not be covered in definition of term 'securities'.

- Due to this ruling, a question may arise as to the applicability of GST on sale of shares of private companies. However, the following aspects need to be considered while assessing whether the shares of the private limited companies can be treated as 'securities' under Section 2(h) of the SCRA and the consequent taxability of transfer of such shares under GST:

  o Under the provisions of the Companies Act, 2013 ('Companies Act'), both private and public companies are entitled to issue securities. The term 'securities' under Section 2(81) of the Companies Act is defined to mean the securities as defined under Section 2(h) of the SCRA. As a result, one may contend that the term 'securities' would also cover securities of a private company.

  o As highlighted above, the Supreme Court in ***Bhagwati Developers Pvt. Ltd. (supra)*** had held that whatever is capable of being bought and sold in a market is marketable. The scope of the term 'marketability' has been examined by the Hon'ble Supreme Court, in various cases pertaining to excise duty, including in ***Camlin Ltd. vs. CCE [2005 (180) ELT 307 (SC)***] wherein it was held that once it is shown that a product has actually been bought, marketability gets established. Applying the ratio of the Supreme Court, in cases where the shares of a private company are being bought, the same would satisfy the criteria of being 'marketable', and consequently, such shares could be considered as 'securities' under the SCRA.

  o Any attempt to interpret Section 2(h) of the SCRA so as to not cover shares issued by a private company would result in anomalous situation whereby the transaction of shares issued by a public company (whether listed or not) would be treated as 'transaction in securities' and hence, not treated as supply whereas transaction of shares issued by a private company could end up being outside the purview of the term 'securities', potentially resulting in it being

treated as supply (leading to question as to whether it would be supply of goods or services), which may not be the intention of the legislature.

- o Lastly, strict interpretation of the definition of the term 'securities' could lead to absurd results. While the definition of the term 'securities' is included in the SCRA as well as CGST Act, the purpose for which both these laws have been enacted is different. SCRA is enacted to prevent the undesirable transactions in securities by regulating the business of dealing therein whereas the GST laws have been enacted to levy and collect tax on supply of 'goods' and 'services'. Hence, it is evident that both the laws operate in different spheres. 'Securities' are specifically excluded from the definition of 'goods' and 'services' under the CGST Act. Basis such exclusion, it can be inferred that it does not seem to be the intention of the legislature to levy tax on the transfer of such financial instruments. Hence, adopting the test of purposive interpretation of law, it can be interpreted that since it may not be the intention of the legislature to levy tax on the sale of securities, the term 'securities' should be interpreted widely and even the shares of a private company should be covered under the definition of the term 'securities', for the purpose of GST laws, and no tax should be charged on the sale of shares of a private company. It is relevant to note that this position seems to have been adopted by the industry, and till date, there does not seem to be any challenge to this position by the GST authorities.

- Basis the above, one may contend that where the shares of a private company can be purchased/acquired, such shares could be treated as being 'marketable', and hence, covered under the term 'securities' under the SCRA. However, there are no clarifications or judicial pronouncements supporting the above contentions and it would be interesting to study the judicial pronouncements on this issue, whenever pronounced.

F. GST implications on transfer of business through Share Acquisition

- In view of the above, in case of transfer of business through Share Acquisition, since the shares of a public/private company are capable of being bought and sold, a position can be taken that such shares could be treated as 'marketable securities' and be covered under the definition of the term 'securities' under Section 2(h) the SCRA Act/Section 2(101) of the CGST Act. Consequently, any transaction involving sale of such shares by the shareholders of the Company being acquired, to the acquirer, would not be subject to GST, being neither 'goods' nor 'services'.

- Since the sale of shares does not amount to supply and no GST can be levied on sale of shares, it now becomes relevant to see whether any ITC needs to be reversed in such cases. Here Section 17(2) of the CGST Act is relevant which provides that where the goods or services or both are used by the

registered person partly for effecting taxable (including zero-rated) supplies and partly for effecting exempt supplies, the amount of ITC shall be restricted to the ITC attributable to the said taxable (including zero-rated) supplies. Further, Section 17(3) of the CGST Act stipulates that the value of exempt supplies (under Section 17(2) of the CGST Act) shall inter alia include transaction in securities.

- In light of the above provisions, the transfer of shares would be construed as an exempt supply under the GST law. Further, the transferor of such shares would be liable to reverse proportionate input tax credit in terms of Rules 42 and 43 of the Central Goods & Services Tax Rules, 2017 ('CGST Rules').

- As a result of the above, the following implications would emerge in the hands of the transferor of shares:

  o **Determining the value of exempt supplies**: As per Explanation below Rule 45 of the CGST Rules, the value of exempt supply would be one percent of the sale value of shares.

  o **Requirement of reversal under Rule 42 and Rule 43 of the CGST Rules:** The eligibility of ITC qua the transferor of shares would be as follows:

    — ITC on goods/services used exclusively for making taxable supplies would be available;

    — ITC on goods/services used exclusively for making exempt supplies of sale of shares (e.g., ITC on transaction related expenses) would not be available; and

    — ITC on goods/services used partly for effecting taxable supplies and partly for effecting exempt supplies would be available on a proportionate basis. However, it would be important to determine, what are these goods/ services which are used to provide both, taxable as well as exempt supplies.

G. Conclusion

- From the aforesaid analysis, the key takeaways on the GST implications on transfer of business of a public/private company through share acquisition are as follows:

  o Shares of a public/private company could be treated as 'securities' under Section 2(h) of the SCRA/ Section 2(101) of the CGST Act;

  o No GST would be leviable on share transfer since sale of securities do not amount to supply under GST law;

  o The sale of shares would be treated as exempt supplies;

  o Value of exempt supply would be 1% of the sale consideration of such shares; and

  o The transferor would be required to reverse ITC attributable to sale of shares in terms of Rules 42 and 43 of the CGST Rules.

H. Other related issue

- While it appears from the above that the transfer of shares may not attract GST, let us now look at an allied issue, which may arise during such transfer of businesses by sale of shares.

- In cases where the transaction involves exit of a promoter, in the agreements entered into for sale of such shares, it is typical to include a condition prohibiting the exiting promoter to conduct the same business or hire the employees of the company being sold for a specified duration (i.e., non-compete and non-solicitation clauses). The issue which now needs to be examined is the taxability of such non-compete or non-solicitation clauses.

- Such non-compete clauses may either have a separate consideration (over and above the price for the shares) or it would be an obligation imposed on the seller at the time of sale of shares, without any specific consideration. Let us look at both the situations separately:

  - o A separate consideration is paid: In this case, it can be said that the seller is providing a separate service, over and above sale of shares. The agreement to non-compete would be a service of 'agreeing to refrain from doing an act', as clarified in circular no. 178/10/2022 dated 3 August 2022. Accordingly, such services would subject to GST. However, in case, the buyer is located outside India, the seller should analyse whether such services can be considered as exports of services and be claimed as zero-rated services.

  - o No separate consideration is paid: In some cases, as a part of the various obligations on the seller in the agreement for sale of shares, such non-compete clauses are also included. In such cases, it can be said to be a part and parcel of the overall transaction for sale of shares, as a condition of sale, without attribution of a separate consideration. In the absence of any consideration or indeed, an intention to provide a service, one may argue that there is no service and no consideration, and consequently, there should not be any tax liability. However, there can be complications when the transaction involves related parties or if the tax authorities seek to impute a part of the consideration for sale of shares towards such non-compete (though there is no specific provision in the law permitting this). This is a judicially untested position as yet and it would be interesting to see the judgments on this, as and when available.

Acquisition of a business by acquisition of Partner's share/s in a Partnership Firm/LLP

A. Introduction

- Acquisition of a Partner's share in a Partnership Firm or LLP (collectively referred to as 'Firm') is a mode of transfer of ownership in a Firm. Here, the acquirer agrees to acquire stake in the Firm from existing partner/s. The relevant provisions and the consequent GST implications on acquisition of a Partner's share in a Partnership Firm and

LLP are similar, and hence, the same have been dealt with simultaneously in this section.

- Unlike the shares of a public/private company, a Partner's share in the firm cannot be transferred. The provisions of section 29 of the Indian Partnership Act, 1932 and section 42 of the Limited Liability Partnership Act, 2008 permit a partner to transfer its right to share profit/loss and to receive distribution from the firm. However, such rights do not result in the assignee becoming a partner in the firm/ LLP and also does not entitle the assignee to participate in the management or conduct of various activities of the firm. Since the intention is to acquire business, the acquirer would seek to participate in the management and such transfer of interest in sharing profit/loss etc. may not be relevant where the intention is transfer of ownership and is not discussed further. To obtain management control, the acquirer should become a partner in the Firm and the transferor/s should retire from the Firm.

- Accordingly, transfer of a Partner's share in a Firm would involve simultaneous occurrence of the following two events:

  o Retirement of existing partner/s in the Firm ('Exiting Partner'); and

  o Introduction of a new partner in the Firm ('Incoming Partner').

  Each of the aforesaid events are accounted for separately in the books of accounts of the Firm. Consequently, the GST implications on each of the aforesaid events should be examined separately.

- In this section, we will examine the GST implications on the transfer of a Partner's share in the Firm.

B. GST implications qua the Exiting Partner

- When a partner retires from a Firm, the Firm pays the settlement amount to the partner. Generally, such settlement amount could be the sum total of amounts lying in the Exiting Partner's capital/current accounts in the Firm.

- The Retirement Deed for the retirement of a partner may inter alia stipulate that the Exiting Partner is foregoing all the rights in the Firm towards the continuing partner/s. Further, in certain cases, the Retirement Deed may provide for various restrictions/conditions such as non-compete, non-solicitation of clients/customers and employees, etc. Therefore, the issue which needs examination is applicability of GST on the amount paid to the Exiting partner.

- To address the aforesaid issue, the consideration payable by the Firm to the Exiting Partner can be bifurcated into the two components viz., amounts lying in Exiting Partner's Capital/Current A/c, and amount paid over and above capital balance. GST implications on each of the aforesaid components are set out hereunder:

  o ***Amounts lying in the Exiting Partner's Capital/Current A/c:***

    — These amounts are acknowledged as a liability in the books of accounts of the Firm. At the time of retirement of the partner, such amounts would be payable to

the partner. Such repayment of a liability is should not attract GST.

- o ***Amounts paid towards Goodwill/ other obligations of the Retirement Deed:***

  - — Here, the issue is about applicability of GST on the amounts paid to the Exiting partner/s over and above the balance in their capital account.

  - — The Exiting Partner can adopt a position that such amount is compensation towards agreeing to refrain from doing an act or to do an act, and for complying with the contractual clauses of the Retirement Deed. In such a scenario, one may adopt a view that such amounts are leviable to GST at the rate of 18%.

  - — There also exists an alternative school of thought that such amounts received by the Exiting Partner may not be leviable to GST, basis the following contentions:

- In the case of ***Amrish Rameshchandra Shah vs. Union of India [2021 (3) TMI 378 – Bombay High Court]*** and ***Gautam Bhattacharya and Yatin Vijaya Patil vs. Commissioner of Central Tax [2022 (3) TMI 230 – CESTAT Bangalore]***, it was held that the partnership firm and its partner are one and the same and that one cannot provide service to self. Accordingly, amounts received by the partner from the partnership firm is just a portion of the profit of the partnership firm, and hence, cannot be subjected to the levy of Service tax. These judgments were in relation to the remuneration received by the partners from the LLP.

- Reference can also be made to the case of ***Mormugao Port Trust vs. CCE [2017 (48) STR 69 (Tri.-Mum.)]*** affirmed by the Hon'ble Supreme Court in 2018 (10) TMI 1675, it was held that "A contractor-contractee or the principal-client relationship which is an essential element of any taxable service is absent in the relationship amongst the partners/co-venturers and joint venture. In such an arrangement of joint venture/partnership, the element of consideration i.e., the quid pro quo for services, which is a necessary ingredient of any taxable service is absent."

- Further, CESTAT Mumbai in the case of ***BG Exploration Production India Ltd. vs. Commissioner of Service Tax (Audit-I) [2021 (10) TMI 306 – CESTAT Mumbai]*** held that mere flow of money by itself is not enough to fasten a Service tax liability. It is obligatory on the part of the Department to show that the said flow of money is a consideration for rendition of a service, in which case alone, there can be a liability to Service tax.

- While the above-mentioned rulings are in the context of the erstwhile Service tax regime, the principles thereof can usefully be applied to the GST regime. Accordingly, unless the documentary evidence showcase that the amounts paid to the Exiting Partner pertains to an independent service supplied to the Firm, it may be contended that GST cannot be levied on such receipts.

C. **GST implications qua the capital contribution by an Incoming Partner**

- Having examined the GST implications on the amounts paid by the Firm to the Exiting Partner, it is worthwhile to examine the GST implications on the amounts brought in by the Incoming Partner and whether the same can be treated as consideration for the services supplied by the Firm to the Incoming Partner.

- In this regard, it is imperative to note that at the time of admission of a partner, an admission deed is entered into, inter alia, stipulating the rights and duties of the Incoming Partner and the payments made by such Incoming Partner in the Firm upon admission.

- Therefore, the issue which is the subject matter of consideration is whether the amounts paid by the Incoming Partner to the Firm at the time of admission in partnership would be leviable to GST.

o Amounts credited to the Incoming Partner's Capital/Current A/c would be acknowledged as a debt in the books of accounts of the Firm. Such introduction of capital is nothing but transaction in money.

  o The above stated view is substantiated by Circular No. 35/9/2018-GST dated 5 March 2018, which had clarified that capital contribution made by a member of the unincorporated joint venture ('UJV') to the UJV is a transaction in money and hence, not leviable to Service tax/GST.

  o While the aforesaid Circular is in the context of Joint Ventures, the principles laid down by the Circular can usefully be made applicable to the Firms. Thus, amounts brought in by an Incoming Partner would be treated as transaction in money, and hence, not subject to GST.

Action points post conclusion of the transaction

Post the transaction, the acquirer should review and identify the new related party relationships, which would arise as a consequence of the transaction and also, the related party relationships, which has come to an end, as a consequence of the transaction, so that appropriate valuation or determination of supply can be made. The acquirer should also align the tax positions of the acquired business with its existing business.

As a concluding remark, it can be said that the acquisition of business by way of share purchase or acquiring the share of a partner in the partnership firm may not generally be subject to GST. Further, there are not many other indirect tax issues involved, which may lead to tax implications or procedural compliances, largely, since the legal entity, which conducts the business, continues to function as it is, without any change. However, the taxability under corporate tax may need significant analysis.

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Dissolution of Firms (including LLP) - GST Implications & Issues

India's ecosystem is full of partnerships and Limited liability companies (which is a hybrid between a partnership firm and a company), owing to its advantage of the simplicity of creation and less hassles relating to statutory compliances, unlike a Company. The functions, roles, and responsibility of the partners in a Partnership firm are governed by the Indian partnership Act, 1932 ('IPA') and an LLP is governed by Limited Liability Partnership Act, 2008.

The key aspects for our discussion in this article are the GST implications that may arise on the dissolution of a partnership firm/LLP *viz*. (a) Liability to GST dues on discontinuance and liability of partners in such case (b) Liability arising on transfer or distribution of Assets and finally (c) Surrender of GST registration.

Liability to GST dues and Liability of Partners

Liability on discontinuance of business

Section 90 of the CGST Act seeks to make all the partners of the firm, jointly and severally liable for any dues payable by the firm whether such tax or interest is determined, or penalty imposed prior to or after discontinuation of business by the firm.

Section 94(1) of the CGST Act specifically deals with the discontinuation of business and provides that:

(i) Where a firm which is a taxable person has discontinued business, the tax, interest, or penalty (hereinafter jointly referred to as 'Tax liability') payable under the CGST Act by the such firm up to the date of such discontinuance may be determined as if no such discontinuance had taken place.

(ii) Every person who, at the time of such discontinuance, was a partner of such firm notwithstanding such discontinuance, jointly and severally, be liable for the Tax liability imposed and payable by such firm irrespective of whether such liability has been determined prior to or after discontinuance.

(iii) The partner will be assessed under the provisions of the law as if the Partner were himself a taxable person

There are also several judicial precedents[1] in the pre-GST era which have held that if tax/penalty was not recoverable from the partnership firm, the same ought to be recovered from the partners.

The general rule as to a partner's liability for acts of the firm is based on the principle of agency and confines the liability only to acts of the firm done while he is a partner. Hence, what is required to be established is whether the act of the firm in respect of which liability is sought to be enforced against a party must have been done while he was a partner. If an act is binding on the firm, every partner will be liable for it. This is irrespective of the fact that a partner was not known as a dormant or a secret partner. The true principle of partnership liability being the existence of an implied agency, it follows that every partner should be liable for all acts of the firm, as was also held in the decision of Madras High Court in ***Sinnaraju Chettair vs. UOI***.

Also, while the liability of a Partner vis-à-vis GST laws is joint and several, the liability inter-se between the partners will be governed by the partnership deed. Section 25 of the IPA lays down the general rule that every partner is liable for all the acts of the firm done ***'while he is a partner'***, and that the liability is both joint and several. The expression 'act of a firm' means any act or omission by all the partners, or by any partner or agent of the firm which gives rise to a right enforceable by or against the firm.

The aspect that a partner is liable ***'while he is a partner'*** has also been recognized by the GST laws in terms of Section 90 of the CGST Act. Section 90 of the CGST Act inter alia states that the firm or the partner retiring from the firm ought to give a written intimation to the Commissioner, within 30 days from the date of its retirement, as regards its retirement from the partnership firm. This is done to restrict the liabilities of the retiring partners to the dues of the firm up to the date of his retirement whether determined or not, on that date. It also provides that any failure to provide such intimation within one month from the date of retirement, would make such retiring partner liable to the firm's dues up to the date on which such intimation is received by the Commissioner.

In so far as a Limited Liability Partnership (LLP) is concerned, on a plain reading of Section 90 of the CGST Act, the same applies to a 'firm' and not to an LLP. The definition of 'person' u/s. 2(84) of the CGST Act lists down a 'firm' and an LLP as separate persons. However, Explanation (i) to Section 94 of the CGST Act specifically provides that a "Limited Liability Partnership" formed and registered under the provisions of the LLP Act, 2008 shall also be considered as a firm. Hence, while on one hand, the liability of a partner in an LLP is restricted to the extent of the partner's capital contribution, on the other hand, the GST provisions provide for a joint and several liabilities. This defeats the very ethos of being registered as an LLP.

GST Liability where IBC proceedings have been initiated against the firm/LLP

Section 93(3) of the CGST Act creates a carve-out from the rule of joint and several liabilities in a situation where proceedings under the Insolvency and Bankruptcy Code, 2016 ('IBC proceedings') have been initiated.

It is to be noted that as per the law settled in the case of ***Ghanashyam Mishra and Sons Private Limited through the Authorized Signatory vs. Edelweiss Asset Reconstruction Company Limited through the Director &***

1. *Sinnaraju Chettair vs. UOI [2000 (126) E.L.T. 522 (Mad.), Gomathinayagam vs. CC [2006 (201) E.L.T. 365 (Tri. – Chennai), ABC Engineering works vs. CCE [2016 (44) S.T.R. 219 (A.P.)*

Ors., once a resolution plan is approved, all claims (including claims arising out of the proceedings initiated by the GST Authorities), not forming a part of the resolution plan, shall stand extinguished. It is also now a settled position that GST and Customs department is classified as operational creditors and are required to submit their claims against corporate Debtors when the insolvency and resolution process is initiated and a public announcement inviting claims is made by the insolvency professional. In this regard, the Central Board of Indirect Taxes and Customs have also issued instructions[2] *inter alia* laying down an SOP for filing claims before the Resolution professional.

Sale/Transfer/Disposal of Business Assets

Another critical aspect that needs to be looked at closely is the transfer/distribution of assets at the time of dissolution of a partnership/ LLP. In this regard, Section 85 of the CGST Act is to be noted that specifically provides that where the partners of a firm transfer their business in whole or in part, by sale, gift, lease, leave and license, hire or in any other manner whatsoever, the firm and the transferee are jointly and severally liable wholly or to the extent of such transfer, to pay the dues from such firm up to the time of such transfer. Further, with effect from the date of such transfer, only the transferee is liable to pay tax on the supply of goods or services or both effected by him.

GST becomes payable in the usual course when there is any sale/transfer of assets to an unrelated third party for consideration. Needless to mention that the GST provisions relating to classification, rate and valuation need to be adhered to. In certain instances, due care is to be taken with respect to certain specific provisions like transfer of capital goods where the liability is either the transaction value or reversal/payment of GST after applying 5% depreciation per quarter considering an asset's life of 60 months.

However, an aspect that needs specific attention is transferred which is otherwise than by way of sale for consideration e.g. assets given by way of gift or assets taken by partners. In this context, one may refer to the decisions in ***Synthetic Suppliers vs. Commissioner of Sales Tax, Mumbai [2010 (5) TMI 764 - Bombay HC], State Of Gujarat vs. Patel Oil Mills [1993 91 STC 25] and Commissioner Of Sales Tax, M.P. V. Khurana And Co. [1980 46 STC 39]*** wherein it was held that he property which is brought into the partnership by the partners when it is formed or which may be acquired in the course of business of the partnership, becomes the property of the partnership and the partner is, subject to any special arrangement between the partners, entitled to his share, upon dissolution of the partnership, in the money representing the value of the property. Upon dissolution of the partnership, all partners are entitled for their respective shares in the property of the partnership as owners. Therefore, there is no question of sale between the partners but the same is a distribution of their own property.

It is noteworthy that as per Section 7(1)(aa) of the CGST Act, the activities or transactions, by a person, other than an individual, to its members or constituents or vice-versa, for cash, deferred payment or other valuable consideration is a supply. The Explanation to said sub-section further states that the person and its members or constituents shall be deemed to be two separate persons and the supply of activities or transactions inter-se

2. *Instruction No. 1083/04/2022-CX9 dated 23.05.2022*

shall be deemed to take place from one such person to another.

Further, as per Schedule I of the CGST Act, any permanent transfer or disposal of business assets where input tax credit has been availed on such assets is liable to GST even if without consideration. In addition, the supply of goods or services or both between related persons is liable when made in the course or furtherance of business.

A partner would constitute a related party and therefore, a combined reading of the aforesaid provisions would indicate that where a partner takes an asset of the firm, there is a supply between the firm and the partner and GST will apply. In such a case, the value must be determined in terms of the GST Valuation Rules . Per the Valuation Rules, the value in a sequence should either be the open market value of the asset or if the same is not available, be the value of supply of goods of like kind or quality or 110% of the cost of acquisition or is to be determined using reasonable means consistent with the principles and the general provisions of Valuation. Where the assets are taken as a set-off against capital lying to the credit of the partner, this could constitute a form of barter and the value can be determined accordingly basis the capital payable which has got adjusted.

The liability to pay GST as above will also apply where assets are sold during dissolution. In this regard, one may refer to decisions in the pre-GST regime where it were held that a business in its entirety cannot be said to be sold in the course or furtherance of business as such sale would leave no business to deal with, therefore, the transfer of assets or stock made on dissolution could not be said to have been undertaken in the course or furtherance of business which is a pre-requisite condition which ought to be satisfied for levy of any VAT. However, the said contention may not apply under GST owing to Entry 4(c) to Schedule II of the CGST Act, which specifically provides that where any person ceases to be a taxable person, any goods forming part of the assets of any business carried on by him shall be deemed to be supplied by him in the course or furtherance of his business immediately before he ceases to be a taxable person, unless—

(i) the business is transferred as a going concern to another person; or

(ii) the business is carried on by a personal representative who is deemed to be a taxable person.

Another important aspect that needs to be kept in mind is liability arising out of non-fulfillment/incomplete fulfillment of export obligations. If any Capital Asset has been obtained under the EPCG scheme, the same is subject to the end-use condition and cannot be disposed off until the export obligation has been completed. In case of non-fulfillment/ partial fulfillment of export obligation, the duty saved at the time of import will be required to be paid along with interest. The firm/LLP will have to also obtain EODC after adducing proof of payment and a No Objection certificate from the customs authorities. It is only after fulfilling the aforesaid formalities that the asset can be disposed of.

One also needs to be mindful of certain payments that could arise out of a dissolution deed e.g., say non-compete fee paid by one partner to another. Such a consideration is

3. Section 15 of the CGST Act read with Rule 28 of the CGST Rules
4. *Paradise Food Court vs. State of Telangana 2017-TIOL-2672-HC-AP-VAT and The Deputy Commissioner of Sales Tax (Law) vs. Dat Pathe [(1985) 59 STC 374 (Ker)]*

likely to attract GST under entry 5(e) of the Schedule II to the CGST Act, which covers treats *"agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act"* as a supply of service.

Accumulated credits

Amongst the assets of the business, there may also be accumulated GST credits. While some of those credits may be utilized to pay liabilities on transfer of assets or other goods, however, the balance may get lapsed.

One could evaluate an option of filing a refund claim of such accumulated credits as on the date of dissolution of the firm. Reliance in this regard can be taken from the decision in ***UOI vs. Slovak India Trading Co. Pvt. Ltd [2007 (1) TMI 556 - SC]*** wherein the Hon'ble Supreme Court allowed a refund of accumulated credit balance on the closure of the factory. However, the Hon'ble Bombay High Court in the case of ***Gauri Plasticulture P. Ltd 2019 (30) G.S.T.L. 224 (Bom.)*** distinguished the judgment of ***Slovak India (supra)*** and denied a refund of credit lying unutilized on the date of closure of the factory.

It is to be noted that Section 54 of the CGST Act provides for situations where a refund can be claimed under the GST Law. Section 54 states that any person claiming a refund of any tax and interest, if any, paid on such tax or any other amount paid by him, may make an application before the expiry of two years from the relevant date in such form and manner as may be prescribed. Further, Section 49(6) of the CGST Act states that the balance in the electronic cash ledger or electronic credit ledger after payment of tax, interest, penalty, fee or any other amount payable under this Act or the rules made thereunder may be refunded in accordance with the provisions of section 54. On a joint reading of both provisions, one could argue that there is no bar from claiming a refund of accumulated credit.

Cancellation of GST Registration

The final aspect would be the applying for cancellation of GST registration of the partnership firm/LLP. The firm can apply to the jurisdictional GST office for cancellation of registration in a case where the business has been discontinued. However, the jurisdictional officer may suspend the registration and not cancel the same during the pendency of any proceedings. Upon completion of the proceedings, the suspension of registration shall be deemed to be revoked and such revocation shall be effective from the date on which the suspension had come into effect.

Further, the firm/LLP is liable to pay an amount equivalent to the credit of input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock or capital goods or plant and machinery on the day immediately preceding the date of such surrender, or the output tax payable on such goods, whichever is higher. For this purpose, the aforesaid details are required to be submitted to the jurisdictional officer in Form GST REG-16 within 30 days of the application for surrender.

Conclusion

It is important for firms/LLP's to ensure that all of the aforesaid compliances are met at the time of dissolution. The surrender of registration post-dissolution does not mean that the liabilities cannot arise subsequently. As already dwelled in detail aforesaid, a partner is jointly and severally liable for any liability even post-dissolution. Separately, ideas around tax optimization such as the appropriate use of credit balance for discharging liabilities arising during dissolution or evaluating refund of accumulated credit should also be examined.

CA Shuchi Sethi

CA Yash Dhadda

Succession of Proprietary Business - GST Implications

Introduction to Sole Proprietorship

A Sole proprietorship is an enterprise owned exclusively by one natural person, in which there is no legal distinction between the owner and the business entity. Sole Proprietorship Business is the simplest business structure in terms of their setup, management, and dissolution. Consequently, it is the most common type of business entity in India. To register a sole proprietorship, one needs following:

— Permanent Account Number (PAN) of an individual under Income Tax Act 1961 (Mandatory)

— A business Name/Trade Name (if intended to be different from legal name of owner)

— A GST Registration Number, (only if threshold is crossed or certain specific transactions are undertaken)

Some key features of Sole Proprietorship Entities which are worth highlighting are as under:

I. Sole Ownership

Only one natural person can be owner of a Sole Proprietorship Entity. The entity may have multiple employees, but owner and management can be only one single person named as "Sole Proprietor" who has complete control over the business management, operations and has the responsibility with authority to make and implement all decisions.

II. Unlimited Liability

Since business is not a separate legal entity, sole proprietor is personally liable for the business' debts and liabilities. He is the only risk bearer and thereby any liability occurring out of that business is his liability.

III. No Perpetual Existence

Under Indian Law(s), a sole proprietorship does not have a perpetual existence, which means the business will immediately come to an end, the moment the sole proprietor dies or becomes insolvent.

The term "Succession" means the act of getting a title or right after the person who had that title or right before has died or is no longer able or allowed to have it. The sole proprietorship business can be succeeded in any of the following ways

A. Death of the Proprietor

B. Proprietor is Alive

a. Transfer through Will

b. Sale of Business

c. Conversion to Partnership Firm/ Company, LLP

Whenever business of a proprietorship entity is succeeded, following instances may occur:

— Legal Ownership of the business gets changed.

— Assets and Liabilities of the business are transferred as it is.

— Business can be continued or maybe closed by successor at his will.

— If it is continued the Trade Name may get changed or existing name maybe continued by the successor at its will.

With context to the provisions of the GST Act(s), in each of the different ways of succession of a Proprietorship Business, the liabilities, procedures, and formalities are different. Same have been discussed as under:

A. Succession due to Death of the Proprietor

With the death of proprietor, legally the business of a sole proprietorship entity comes to an end. However, under the provisions of however the GST law provides a facility whereby the legal heir(s) can continue the business if they desire, apart from choosing to discontinuing the same. There are detailed procedures with instructions given under the Act(s) and Rule(s) as to how such succession in either case can be done.

A.1. Cancellation of Existing GST Registration of the deceased Sole Proprietor and new GST Registration by Legal Heir(s)

As per Section 29(1) of the Act legal heir(s) of a deceased registered person can file an application for cancellation[1] of existing GST Registration through GST Portal. However before filing such application, legal heir(s) will have to get themselves registered as Authorized Signatories. To be added as Authorized Signatories amendment in registration details are required which cannot not be done by the legal heir(s) themselves because as per Section 28 read with Rule 19 only registered person can apply for amendment on GST Portal. Since said registered person is not alive, hence the legal heir(s) will have to approach the jurisdictional proper officer for the given step. The proper officer may require the "Legal Heirs" to prove that they are the legal heirs of the deceased as defined in the personnel law(s) as enforced on the date in India. Documents that may be required to prove person(s) as legal heir(s) (only illustrative)

— Identity Card having name of both deceased and legal heir. E.g.- PAN, Aadhaar etc.

— Id Proof of the deceased

— Death Certificate of deceased

1. Form REG-16 on GST Portal

- — Succession Certificate
- — NOC if there are multiple legal heirs in favor of the one being applied for Authorized Signatory

It must be ensured before filing the application for cancellation that all GST returns have been filed of the deceased. As per the provisions of the Act, application for cancelation must be made within 30 days of date of death with reason of cancelation as "death of proprietor". However as per clarification[2], the 30-day time-limit can be applied liberally.

Final return[3] is also required to be filed within 3 months from the later of the either date of cancellation order or date of cancellation as approved by proper officer.

If legal heir(s) intend to continue the business of the deceased sole proprietor, then before undertaking above process of applying for cancellation, they must first apply[4] for registration under Section 22(3) of the Act. While filing such application, the legal heir(s) is required to mention the reason to obtain registration as "death of the proprietor. Subsequently in the cancellation application, the GSTIN of transferee (legal heir(s)) to whom the business has been transferred is also required to be mentioned to link the GSTIN of the transferor (deceased sole proprietor) with the GSTIN of transferee.

The new registration is required to be taken with effect from the date of such transfer or succession. Even if business activities are not re-initiated or are halted for some time from date of death of sole proprietor, and are resumed after some gap (attributable to any personal or procedural reason(s)), the said "date of succession" shall continue to be the date of death of the sole proprietor only. The clarification[2] only hints at relaxing the timeline for filing of application for cancellation of existing registration. But there is no clarification/instruction for relaxing the timeline for seeking new registration.

A.2. Tax Liability & Incidence on Legal Heir(s) due to death of Sole Proprietor

As per Section 93(1)(b) of the Act in case any due liability of GST remains unpaid even after the death of proprietor and the legal heir(s) have opted for closure/discontinuance of business, then the legal heir(s) shall be liable to pay the demand of GST along with interest and penalty out of the estate of the deceased (i.e. the property he owned when he died) to the extent to which the estate can meet the charge.

However as per Section 93(1)(a) of the Act, where business is being continued by legal heir(s) and any liability of GST along with interest and penalty is due for the period when the business was carried on by the deceased, then the legal heir(s) are liable to pay the whole amount without any limitation of the capability of estate of the deceased.

The precise reason for such differentiation in extent of liability casted upon legal heir(s) is

2. Circular No 69/43/2018-GST dated 26.10.2018
3. Form GSTR-10 on GST Portal
4. Form REG-01 on GST Portal

attributable to understanding (as clarified in circular also[5]) that in case of death of sole proprietor when the business is continued by any person being transferee or successor of business, it has been to be construed as transfer of business[5].

Further, provisions of section 85(1) of the Act, hold the transferor and the transferee/successor as jointly and severally liable to pay any tax, interest, or any penalty due from the transferor in cases of transfer of business "in whole or in part, by sale, gift, lease, leave and license, hire or in any other manner whatsoever".

But due death of the sole proprietor, since he cannot be held liable for any dues, the provisions of Section 93 of the Act empower the revenue to shift liability and recovery upon the legal heir(s) without restriction to estate of deceased sole proprietor.

However, the provisions of Section 93 of the Act specify to recover, not only the amount determined before the death of transferor, but even also those determined after his death and have remained unpaid. Though machinery provisions to implement and recover the same appears to be missing in the Act (analyzed subsequently).

A.3. Transfer of Unutilized Input Tax Credit

Section 18(3) of the Act allows the registered person to transfer the unutilized input tax credit lying in his electronic credit ledger to the transferee in the manner prescribed in rule 41 of the Rules, where there is specific provision for transfer of liabilities. Thus, the legal heir(s) firstly in capacity of authorized signatory of deceased sole proprietor files FORM GST ITC-02[6] on the common portal with a request for transfer of unutilized input tax credit lying in electronic credit ledger of said deceased proprietor to the transferee (i.e., its new registration in own capacity as owner).

Procedurally it is relevant that FORM GST ITC-02 is be filed by the legal heir(s) before filing the application for cancellation of such registration. Later, upon acceptance by the legal heir(s) as transferee/successor (from new registration), the un-utilized input tax credit specified in form gets credited to their electronic credit ledger.

A.4. Can Liability to pay tax be determined upon Legal Heir(s) after death of the proprietor?

According to Section 29(3) of the Act, for any period prior to the date of cancellation, the cancellation of registration in itself does not affect the liability of the person to pay tax and other dues under this Act, even if such tax and other dues are determined after the date of cancellation. The said provision is applicable for all types of cancellation applications and is not only restricted to cancellation due to reason of death of the registered person.

5. Para 3c of Circular No 96/15/2019-GST dated 28.03.2018
6. Form GST ITC-02

However, as such tax and other dues cannot be enforced upon a deceased person, the provisions of Section 93(1) of the Act, which is applicable specifically in case of death of a proprietor, holds the legal heir(s) is liable to pay tax and other dues even if determination of same is done after death of the proprietor.

As per Section 2(11) of the Act, 'assessment' means determination of tax liability under the law and includes self-assessment, re-assessment, provisional assessment, summary assessment and best judgment assessment. Such assessments are subject to adjudication procedure which involves observance of principles of natural justice. The person who is assessed is called assessee (i.e., taxable person) and the person who assessees is called adjudicating authority.

The provisions of adjudication are given under Section 73 and 74 (as the case may be) of the Act. These provisions specifically only allow to serve Show Cause Notice upon the person chargeable with tax. As per charging Section 9(1) of the Act, person chargeable with tax is called taxable person. As per definition of taxable person in Section 2(107) of the Act, a taxable person must be a person first. Definition of person given under Section 2(84) of the Act includes only an individual but does not include legal representatives of deceased. Further use of present tense in the definition indicates that person referred to can only be living person. Thus, effectively there is no machinery provision under the Act to issue a notice for adjudication of legal representatives of deceased. In absence of same, demand of tax and other dues cannot be confirmed without issuance of Show Cause Notice and hence no assessment can be done for determination of tax.

The given understanding has been confirmed in case of ***Shabina Abraham & Others vs. Commissioner***[7, 8], where it has been held by Hon'ble Supreme Court that the assessment proceedings cannot continue against the legal representative/estate of a sole proprietor after he is dead in the absence of any machinery provision under the law. The taxation statute must be interpreted considering what is clearly expressed. It cannot imply anything which is not expressed. It cannot import provisions in the statute to supply any assumed deficiencies. The case pertains to period 1983 to 1985.

Thus, no Show Cause Notice can be issued to a deceased person. If done so, it cannot be treated as a rectifiable defect under section 160(1) of the Act and notice will have no validity. In case of ***C.I.T., New Delhi v. M/s. Spice Enfotainment Ltd***[9] Hon'ble Supreme Court affirmed the decision of the Hon'ble Delhi High Court where it was held that the framing of assessment against a non-existing entity/person goes to the root of the matter which is not a procedural irregularity but a jurisdictional defect as there cannot be any assessment against a "dead person".

7. Citation: (2015) TIOL 159 (SC)
8. Citation: 2012 (281) E.L.T. 64 (Kar.)
9. Order dated 02.11.2017 in Civil Appeal No. 285 of 2014

Further even if a Show Cause Notice has been already issued upon a sole proprietor in respect of business carried out by him, but before passing of the order for confirmation of demand of tax and other dues, the said individual dies, then no demand of tax can be confirmed upon the legal representative due to above mentioned principles.

It effectively means that though provisions of Section 29(3) and 93(1) of the Act requires legal representative to pay tax and other dues pertaining to the deceased person, but due to lack of mechanism in the Act to initiate or to continue or to conclude the assessment upon those legal heir(s) in capacity of assessee of said deceased person after the death of said sole proprietor, such tax and other dues cannot be fastened irrespective of the fact that business is carried or discontinued by the said legal heir(s).

Only such liability of tax and other dues which was already assessed upon an individual before his death can be recovered in accordance with provisions of Section 93(1) of the Act.

Further it is also relevant to note that provisions of Section 83(1) of the Act regarding the provisional attachment of bank account and other assets to protect revenue's interest can be made applicable on a taxable person. As already explained, legal heir(s) do not step into the shoes of taxable person in representative capacity of deceased person, any action of provisional attachment against them shall be unlawful.

A.5. Can there be a liability to pay tax in respect of credit held in stock, capital goods etc. held on the date of cancellation due to death of proprietor?

Provisions of Section 29(5) of the Act requires every registered person whose registration is cancelled to pay an amount equal to the credit of input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock or capital goods or plant and machinery on the day immediately preceding the date of such cancellation or the output tax payable on such goods whichever is higher. The mechanism to calculate the same has been given under Rule 44 of the Rules.

The said provisions cannot be made applicable in case of death of a sole proprietor because the above provision requires the payment to be done by a registered person. As registered person ceases to exist (due to death), there is no mechanism to assess the given liability upon the legal heir(s) of the deceased person (as discussed above).

Even in addition to above, in case the business is continued by legal heir(s), as on the date of death, the business is transferred by way of succession (also date of cancellation) and thus there exists no stock of raw material, semi-finished goods, finished goods or capital goods. In that case the amount to paid shall be otherwise Nil.

A.6. Whether activity of disposal of business assets by legal heir(s) without intending to continue said business be treated as Supply of goods in accordance with Clause 4 (c) of Schedule 2 under Section 7(1A) of the Act?

One may alternatively argue that provisions of Clause 4(c) of Schedule II (Transfer of business Assets) under Section 7(1A) of the Act get triggered if business is not carried by

legal heir(s) on death of the sole proprietor and assets of business are sold/disposed by them after death of sole proprietor. The said clause is read as under

"*where any person ceases to be a taxable person, any goods forming part of the assets of any business carried on by him shall be deemed to be supplied by him in the course or furtherance of his business immediately before he ceases to be a taxable person, unless-*

i. the business is transferred as a going concern to another person; or

ii. the business is carried on by a personal representative who is deemed to be a taxable person."

However, the said provision is not applicable in given case because it assumes the sole proprietor of business to be the supplier who is deceased in given case. Since he is not alive hence the concept of supply gets defeated at the outset. Also, in given case the legal heir(s) when they do not intend to carry on the said business, their activity of selling goods is in a personal capacity but is not on behalf of deceased person. Hence same cannot treated as supply of goods in course of business and hence cannot be levied to tax.

B. Succession due to Transfer by Will/Sale of Business/Conversion to Partnership Firm/Company, LLP

In other ways of succession, where sole proprietor is alive, the transfer of business is out of free desire between the sole proprietor of business and other parties, culminating into a contractual arrangement which can be legally enforced.

Thus, in all these cases, the succession of business results in transfer of business as a going concern to the other party. This can be executed by way of writing a will for legal heir(s) or by entering into business transfer agreement with a buyer or by converting the business into other constitutions like firm or company etc.

In all the given cases, the transfer of business may happen through a slum sale or itemized sale of items of business (as a whole). Once business as whole is transferred to other party it shall be treated as transfer of a going concern.

Whether transfer of business is as a going-concern or not can be determined by one of the test as laid down in case of ***Jayaprakash Shamsundar vs. Laxminarayan Murlidar***[10]. In given case it was held by the Hon'ble Bombay High Court that one test of determining as to whether the business is a going concern is to find out whether the assignee after the assignment would be able to carry on the business which was being carried out in the suit premises by the assignor. If there was a stock-in-trade in the premises, it would provide some indication that there was a business which was a going concern.

10. Citation: AIR 1983 Bom 364

Though transfer of a going concern is treated as an exempt supply of service under GST[11] but same may not fall within the scope of supply at all as the activity of transferring business cannot be constituted as activity in course of or furtherance of business. The same view has been given in case of ***Paradise Food Court vs. The State of Telangana by Hon'ble Andhra Pradesh High Court***[12]. Thus, there can be no tax on transfer of business as going concern by way of will, sale or conversion.

However, the provisions of Section 85 of the Act i.e., joint and several liability of sole proprietor as transferor and receiver as transferee shall be there. In given case, unlike in case of succession due to death of proprietor, the tax liability can be determined upon the sole proprietor even after the date of transfer due to any of the given modes of succession.

Further, the provisions of Section 29(3) of the Act, unlike succession in case of death of proprietor shall also be enforceable here and the sole proprietor shall be required to pay amount equal to the credit of input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock or capital goods or plant and machinery on the day immediately preceding the date of such cancellation or the output tax payable on such goods whichever is higher.

Further the provisions of Section 18(3) of the Act shall also be applicable, and the sole proprietor is allowed to transfer the balance of unutilized input tax credit to the successor's Electronic Credit Ledger by filing of Form ITC-02 on the common portal.

It is to be noted that in given cases of succession, there is no requirement to add any legal representative or legal heir(s) to carry out the formalities of cancellation of registration or transferring of unutilized ITC through common portal.

11. Entry 2 of N.N 12/2017-CT (Rate) dated 28.06.2017
12. Citation: 2018 (16) G.S.T.L. 361 (A.P.)

"You may sit down and listen to me by the hour every day, but if you do not practice, you will not get one step further. It all depends on practice.."

— *Swami Vivekananda*

Ranjeet Mahtani
Advocate

CA Arindam Chatterjee

Insolvency and Liquidation – GST issues

Background

The Insolvency and Bankruptcy Code 2016 ("IBC" or "Code") is the bankruptcy law of India which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy. The Insolvency and Bankruptcy Code, 2015 was introduced in the Lok Sabha in December 2015; it received the assent of the President of India on 28th May 2016 and certain provisions of the Code have come into force from August 2016. The Code is designed as a one-stop solution for resolving insolvencies which previously was a long process that did not offer an economically viable arrangement.

One of the important objectives of the Code is to bring the insolvency law in India under a single unified umbrella with the object of speeding up of the insolvency process. As per the data available with the World Bank in 2016, insolvency resolution in India took 4.3 years on an average, which was much higher when compared with the United Kingdom (1 year), USA (1.5 years) and South Africa (2 years) - ***Innoventive Industries Ltd. vs. ICICI Bank and Anr. MANU/SC/1063/2017: (2018) 1 SCC 407.***

The scheme of the Code is to ensure that when a default takes place, in the sense that a debt becomes due and is not paid, the insolvency resolution process begins. Default is defined in Section 3(12) in very wide terms as meaning nonpayment of a debt once it becomes due and payable, which includes nonpayment of even part thereof or an installment amount. For the meaning of "debt", Section 3(11) is relevant, which in turn explains that a debt means a liability of obligation in respect of a "claim" and for the meaning of "claim" and go back to Section 3(6) which defines "claim" to mean a right to payment even if it is disputed. The Code gets triggered the moment default is of rupees one lakh or more (Section 4) - ***Innoventive Industries Ltd. vs. ICICI Bank and Anr. MANU/SC/1063/2017: (2018) 1 SCC 407.***

The scheme of the Code therefore is, to make an attempt, by divesting the erstwhile management of its powers and

vesting it in a professional agency, to continue the business of the Corporate Debtor ("CD") as a going concern until a resolution plan is drawn up. Once the resolution plan is approved, the management is handed over under the plan to the successful applicant so that the CD is able to pay back its debts and get back on its feet- ***Innoventive Industries Ltd. vs. ICICI Bank and Anr. MANU/SC/1063/2017: (2018) 1 SCC 407.***

GST and IBC

Any tax liability of Goods and Services Tax ("GST") relates to an economic transaction in goods and services. In so far as there is a supply of goods and services etc. or both, GST is applied and while the taxpayer is the supplier, the burden of tax is typically, on the consumer.

As such, in a proceeding under the Code, there is a moratorium, revival plan, discussions by various stakeholders and eventually restructuring of the company under IBC which ordinarily has no touchpoints under the GST law. In the alternate, there may take place a liquidation under the provisions of the Code, which too is fashioned as a going concern. This article aims to summarize and provide a bird's eye view of the GST implications and touchpoints for a juridical person under the IBC.

The Central Board of Indirect Taxes and Customs ("CBIC") clarified vide Circular no. 134/04/2020 GST dated 23rd March 2020 ("March 2020 Circular") that in accordance with the provisions of the IBC and various legal pronouncements on the issue, no coercive action can be taken against the Corporate Debtor (CD) with respect to the dues for the period prior to the insolvency commencement date.

Importantly, the taxation dues of the period prior to the commencement of the Corporate Insolvency Resolution Process ("CIRP") will be treated as 'operational debt' and claims may be filed by the proper officer before the NCLT in accordance with the provisions of the IBC. Therefore, the tax officers shall seek the details of supplies made/received and total tax dues pending from the CD to file the claim before the National Company Law Tribunal ("NCLT").

Interim Resolution Professional ("IRP") and Resolution Professional ("RP")

Under an IBC proceeding, an IRP/RP has the responsibility for managing affairs including statutory compliances of the CD. One of the responsibilities includes filing of periodic returns and payment of taxes. However, most CDs defaulted in the filing of GST returns and/or payment of dues at the commencement of CIRP. This made it impossible for IRP/RP to file GST returns and discharge dues for the CIRP period. Practically, in some cases, the GST department directed acceptance of GST returns in hard copies from the IRP/RP, although the GST regime was and is essentially an electronically administered tax regime; there was no uniform approach across the country, and so IRPs/RPs struggled to comply with the filing requirements of GST returns and payment of taxes.

Considering the above challenges, the 39th GST Council meeting held on 14th March 2020 deliberated and provided its recommendations. One of the important decisions was related to the rules pertaining to entities undergoing CIRP under the IBC. Based on the Council's decision, the CBIC, vide notification no. 11/2020 dated 21st March 2020 ("Notification"), notified special procedures under GST related to new registration, filing of returns, and payment of tax dues for the CIRP period under the Central Goods and Services Tax Act, 2017 ("CGST Act, 2017") and the rules made thereunder ("CGST Rules") for the CDs who are undergoing CIRP under the provisions of the IBC, and the management of whose affairs are transferred to the IRP/RP.

The March 2020 Circular clarified various issues under the GST law for companies under IBC. Various State Governments have released their clarifications/circulars in relation to procedures to be followed in the case of companies undergoing CIRP under the IBC. One such prominent circular was issued by the Commissioner of Commercial Taxes (Karnataka) Bengaluru bearing no. GST l5/2020 dated 28th December 2020 ("KGST Circular").

Separate GST registration

A practical hurdle that arose when an IRP/RP attempted to file returns, pay tax, and claim ITC was that the past period tax liabilities were expected to be cleared/paid and then ITC used for the current period. This meant that RP's could not pay tax and/or claim ITC for the CIRP period where the CD's had not discharged past tax liabilities. The following illustration elaborates the situation.

Enterprising Ltd. goes into CIRP and a resolution professional takes over. On the date of commencement of the CIRP, ABC Ltd had pending GST dues of Rs. 20 crores. Now, during the CIRP period, the RP makes outward supplies and charges GST on the same; he makes purchases too, paying GST to the vendors. Upon attempting to file returns and pay tax, there is an issue in as much as the balance in the electronic cash ledger is first utilized to clear the pending dues of the CD, post which the regular return can be filed. The RP is unable to file the GST returns without first paying the earlier dues and clearing the baggage, although a moratorium is in place.

Accordingly, the IPR/RP was unable to pay GST dues during the CIRP period and file periodical returns. In essence, the burden of the past dues continued to spill over during the CIRP period as well.

To combat these situations, the scheme of new registration for the RP/IRP was introduced. A registered person (referred to as erstwhile/existing registered person), who is CD under the provisions of IBC and presently undergoing CIRP, shall be liable to obtain new registration (referred to as newly registered person) in each of the states/UTs where it was registered earlier, within 30 days of the appointment of IRP/RP and in case, where the IRP/RP was appointed prior to the issuance of this notification, then within 30 days of the issue the notification.

The CBIC further clarified that the existing registration of an entity for which CIRP has been initiated should not be canceled. If required, the proper officer ("PO") may suspend the registration. However, where the registration of an entity undergoing CIRP has been canceled already and the period of revocation of cancellation (i.e., 30 days from the date of service of cancellation order) has not yet lapsed, then such cancellation order needs to be revoked.

The time limit of 30 days for obtaining new GST registration is short and some issues persist. At the commencement of the CIRP, IRP is appointed, and soon after an RP comes into place. Besides, after its appointment, an IRP is engaged in arranging a meeting of the creditors, consolidating information, and in several cases, their appointment is also not yet ratified. In certain cases, the IRP is succeeded by a new RP, and in a short timeframe, which raises doubts as to who should obtain the GST registration. The IRP/RP will be liable to furnish returns, make payment of tax and comply with all the provisions of the GST law during CIRP period. The IRP/RP is required to ensure that the first return is filed under section 40 of the CGST Act, 2017 for the period beginning the date on which it became liable to take registration till the date on which registration has been granted.

While the requirement of the scheme of separate registration for the IRP/RP is innovative and commendable, it deserves a revisit on the timelines front.

Availing ITC by the IRP/RP and refund of amount in the cash ledger

The new registration (IRP/RP) is allowed the benefit of claiming past ITC. IRP/RP can, in the first return to be filed by him/her, avail tax credit on invoices covering the supplies of goods or services received since his/her appointment as IRP/RP but, bearing the GSTIN of the CD. ITC can be availed even though the same is not appearing in the Form GSTR2A of the new registration. Further, the time limit provided in Section 16(4) of the CGST Act, 2017 (which concerns the timeline to avail ITC until September or November following March) will also not apply in such a situation. The other conditions provided in Chapter V of the CGST Act, 2017, and the rules made thereunder will apply. It is highlighted that these relaxations operate only in respect of the first return to be filed by the IRP/RP, and not subsequent returns.

As regards outward supplies made by the CD, there is no ambiguity on the eligibility of ITC (GST charged on supplies made by the CD before the CIRP) nor, for the supplies made by the IRP/RP under the new GST registration that it obtains after coming into place. For the interim period i.e. after the date of appointment of IRP/RP but before the new registration has been granted, there arose doubts on the eligibility of ITC charged on such invoices (issued by the CD) since the invoice bears the GSTIN of the erstwhile registered person (CD) but, is issued under the hand of the IRP/RP. The March 2020 Circular clarifies that the customers receiving such supplies will be eligible to

avail the ITC of the GST charged by the IRP/RP using the GSTIN of the CD, subject to fulfillment of other conditions in the GST law.

These procedures are not applicable for those CDs, who have furnished the statement of outward supplies (i.e., Form GSTR1) and consolidated return of inward and outward supplies (i.e., Form GSTR-3B) for all the tax periods prior to the appointment of IRP/ RP.

There is a provision of a facility that any amount deposited in the cash ledger by the IRP/RP, in the existing registration of the CD, from the date of appointment of the IRP/RP to the date of grant of new registration (IRP/RP), can be claimed as refund and thereby east the cashflows for smooth operation of the corporate entity.

After CIRP

An important issue arising from this scheme of GST registration of the IRP/RP is the permanency of the new registration. On a bare perusal of the Notification, it can be inferred that the new registration is a temporary arrangement and seeks to create a break for the CIRP period.

The IBC proceedings may lead to any one of the following possibilities/outcomes:

a. The CD is revived under a resolution plan

b. The CD goes into liquidation

c. The CIRP proceedings are following the process of Section 12A of the Code.

d. The CIRP initiation itself may get reversed by Tribunal or Court.

In respect of ‘a’, ‘c’, and ‘d’ above, the question that remains unaddressed is the revival or resurrection of the CD's original GSTIN and the transition from the IRP/RP’s registration to the CD's registration. As a corollary, the GST registration granted to the IRP/RP should be canceled in due course. While the GST registration scheme provides for the assumption of responsibilities by the IRP/RP (transfer of operations from the CD to the IRP/RP) and thereby compliance burden on the IRP/RP, what the scheme has not done is clearly define the transition steps and process back to the CD. This is perhaps an area worthy of dovetailing and clarification.

Rainbow Papers Limited – Supreme Court

On this subject, a topical aspect is the judgment of the Supreme Court in the case of ***State Tax Officer vs. Rainbow Papers Limited (Civil Appeal No. 1661 of 2020, dated 06th September, 2022).*** The Apex Court held that if the resolution plan ignores statutory demands payable to Government or a legal authority, it (plan) cannot be said to be in conformity to the provisions of IBC, and so should be rejected. In that case, the Court held that Section 48 of Gujarat Value Added Tax Act, 2003 which provides for a nonobstante clause for first charge on the property of a dealer in respect of any amount payable by the dealer on account of tax, interest, penalty etc. is not inconsistent with IBC and so, the Government will fall under “secured creditor” for the liquidation process – thus moving up a couple of

notches in the waterfall mechanism, for payments. Factually, and as was recorded by the NCLAT in its order, the NCLT noticed that the Tax Department approached the RP on 22nd October, 2018 whereas the Resolution Plan dated 26th May, 2018 along with an addendum of 05th June, 2018 was approved by the Committee of Credits (Resolution Plan), and thus the claim was made by the Tax Department at a much belated stage not only before the RP but also the NCLT.

A perspective is that the situation is different in the GST regime since the provisions of GST recovery are subject to the IBC and hence IBC should have an overriding effect.

Nonetheless, the fact that outstanding dues not claimed by the Tax Department under the IBC but, appearing in the financial statements are to be considered (by the RP) while calculating dues payable, deserves to be noted by all professionals involved in IBC proceedings; failure to do which may result into the resolution plan being held as not in conformity with the statutory requirements (IBC).

Company under liquidation

A resolution plan may not fructify and consequentially, the CD could be liquidated. The Supreme Court in ***Swiss Ribbons Pvt. Ltd. & Anr. vs. Union of India (2019) 4 SCC 17 (dated 25th January, 2019)***, declared the law that "the Preamble gives an insight into what is sought to be achieved by the Code. The Code is first and foremost a Code for reorganization and insolvency resolution of corporate debtors...maximization of the value of the assets of such persons so that they are efficiently runs going concern is another very important objective of the Code...What is interesting to note is that the Preamble, does not, in any manner, refer to liquidation, which is only availed of as last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. *Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern."* The NCLAT in ***Vishisth Services Limited vs. SV Ramani (Company Appeal (AT) (Insolvency) No. 896 of 2020, dated 11th January, 2022)*** (issue as to whether sale of CD as a going concern in liquidation proceedings includes its liabilities) held that sale as a going concern means a sale of assets as well as liabilities and not assets sans liabilities if it is arranged on as is where is basis. It is noteworthy that the liabilities are settled in accordance with Section 53 of the Code.

In case of a Company under liquidation or if the CD slips into liquidation, a person may be appointed as receiver of any assets of the Company ("liquidator"). In liquidation proceedings, the sale of the CD on a going concern basis is generally arranged on an "as is where is" basis, and the Liquidation Regulations do not contemplate submission of any plan/ scheme for acquisition/bidding of the CD, whereas the auction terms apply. Since the liquidation proceedings, and indeed sale/ transfer is on a going concern basis, there will not arise GST implications, ordinarily. The scheme for liquidation deserves to be carefully scrutinized for any exclusions or

diversions, such that it may not be viewed as a going concern transfer and thereby give rise to GST being applied.

Section 88 of the CGST Act, 2017 provides that the liquidator, shall, within thirty days after his appointment, give intimation of his appointment to the Commissioner having jurisdiction over the registration. The Commissioner shall within three months from the date on which he receives intimation of the appointment of the liquidator, notify the liquidator of the amount which in the opinion of the Commissioner would be sufficient to provide for any tax, interest or penalty which is then, or is likely thereafter to become, payable by the company. The KGST Circular clarifies that the authorities who have pending arrears from the Company being wound up as on the date of commencement of liquidation shall submit the claims to the liquidator in the prescribed form within 30 days from the date of commencement of liquidation process. It further clarifies that authorities shall file the claims afresh before the liquidator within prescribed time notwithstanding filing of claims during CIRP, and even if such claims were admitted in full by the IRP/RP.

It is highlighted that Section 88(3) of the CGST Act, 2017 places an onus on the directors of a private company in liquidation. As per Section 88(3) of the CGST Act, 2017, the director of a private company being wound up is jointly and severally liable for the payment of any tax, interest or penalty determined under the CGST Act, 2017 on the company for any period, which cannot be recovered from the Company, unless the director can showcase that the nonrecovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company.

"You may ask, "Who wrote the Vedas?" They were not written. The words are the Vedas. A word is Veda, if I can pronounce it rightly. Then it will immediately produce the [desired] effect."

— *Swami Vivekananda*

"It is better to be violent, if there is violence in our hearts, than to put on the cloak of non-violence to cover impotence. Violence is any day preferable to impotence. There is hope for a violent man to become non-violent. There is no such hope for the impotent."

— *Mahatma Gandhi*

CA Milan Mody

HOT SPOT
AQMM – One more step towards enhancing Audit Quality

Good audit quality is imperative for the audit profession to regain the confidence and trust of various users of financial statements. There is a need to bridge the expectation gap by the auditing fraternity vis-à-vis regulators and other stakeholders.

Audit quality is a complex and a subjective matter, however this has not deterred Institute of Chartered Accountants of India (ICAI) in addressing this topic. Accordingly, the Audit Quality Maturity Model (AQMM) was launched in July 2021 by the Centre of Audit Quality formed under ICAI.

This is in addition to the various steps taken on audit quality by various regulators and ICAI like Financial Reporting Review Board, Quality Review Board, Peer Review Board, constitution of National Financial Reporting Authority, etc. Rotation and compulsory joint audit in case of large NBFCs are other initiatives taken to improve the audit quality.

In August 2022 ICAI has announced that the AQMM Rev v1.0 would be mandatory for certain set of firms from 1st April 2023. The firm to whom it would apply include those who are auditing listed entities, bank (excludes branch auditors) and insurance companies.

AQMM is a self-evaluation model based on well researched set of Audit Quality Indicators. It will help firm assess the current maturity level and would provide a road map for improvement in audit quality. In that sense it is also a capability building measure.

The evaluation model is divided into three broad section with each having multiple subsections and competency dimensions. Standardisation of various documents, use of checklist, time sheet and analysis of budgeted and actual time spent on each attest assignment, audit practice manual, use of technology, negative remarks by quality review board quality, control of audit engagement (SQC1) and human resources management are some of the key aspects which are covered under in the detailed questionnaire. The sections and sub section thereon are as under:

1. Practice Management – Operations (total maximum score 280)

    a. Practice areas of the firm

    b. Work flow – practice

    c. Quality review manual / audit tool

    d. Service delivery – effort monitoring

e. Quality control for engagements

f. Benchmarking of service delivery*

g. Client sensitisation

h. Technology adoption

i. Revenue, budegeting and pricing

2. Human resource management (total maximum score 240)

   a. Resource planning and monitoring as per firm's policy

   b. Employee training and development

   c. Resource turnover and compensation management**

   d. Qualification skill set of employees and use of experts

   e. Performance evaluation measures carried out by the firm

3. Practice management – strategic/ functional (total maximum score 80)

   a. Practice management

   b. Infrastructure – physical and others

   c. Practice credentials

* negative scoring under this head

** maximum weightage

Interpreting the scores

Up to 25% in each section	Level 1 Firm	Firm is very nascent - will have to take immediate steps to upgrade its competency or will be left lagging behind
Above 25% to 50% in each section	Level 2 Firm	Firm has made some progress - will have to fine-tune further to reach the next level of competency
Above 50% to 75% in each section	Level 3 Firm	Firm has made substantial progress - will have to fine-tune further to reach the highest level of competency
Above 75% in each section	Level 4 Firm	Firms that have made significant adoption of standards and procedures - should focus on optimising further

As a good practice, once the assessment is done a plan should be put in place for the firm to move to the next level of maturity and thereafter ensure that there is continuous monitoring at engagement/ firm level so that maturity level does not drop. As it is said 'excellence is not a destination it is continuous journey that never end'

The level as achieved by the firm through self-evaluation using AQMM should not be publicized or mentioned in any public domain e.g. on professional documents, visiting cards, letterheads, or signboards, etc. as it may amount to solicitation. However, the level achieved by the firm based on the scores would be shared with the peer reviewer and post review the same would also be hosted on the ICAIs website.

After the first review, the subsequent reviews shall necessarily be aligned to the peer review cycle.

Audit quality is a universal topic and ICAI has done well in addressing this issue on time. A beginning has been made in the right direction.

Keshav B. Bhujle
Advocate

DIRECT TAXES

Supreme Court

1 ***Checkmate Services P. Ltd. and Ors. vs. CIT; [2022] 448 ITR 518 (SC): Dated 12/10/2022***

Business expenditure — Deduction only on actual payment — Contributions to employees' welfare funds such as provident fund and employees' state insurance — Distinction between employer's contribution and employees' contribution — Employees' contribution is money held by assessee-employer in trust — Is income of assessee unless paid into fund by due date — "due date" is date prescribed by enactment governing fund in question — Deductible only if deposited in respective fund by that date: ITA, 1961, Ss. 2(24)(x), 36(1)(iv), (va), 43B, SCH. IV, R. 2(C): A. Y. 2009-10

In these appeals, the common question involved is with respect to the interpretation of section 36(1)(va) and section 43B of the Income-tax Act, 1961, and whether the appellant-assessees are entitled to deduction of amounts deposited by them towards contribution in terms of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952, the Employees' Provident Funds Scheme, 1952, the Employees' State Insurance Act, 1948, the Employees' State Insurance (Central) Regulations, 1950 or any other provident or superannuation fund.

The Assessing Officers had ruled that the appellants had belatedly deposited their employees' contribution towards the employees' provident fund and employees' State insurance, considering the due dates under the relevant Acts and Regulations. Consequently, the Assessing Officer ruled that by virtue of section 36(1)(va) read with section 2(24)(x) of the Income-tax Act, such sums received by the appellants constituted "income". Those amounts could not have been allowed as deductions u/s. 36(1)(va) of the Income-tax Act when the payment was made beyond the relevant due date under the respective Acts. In other words, as per the Assessing Officer, as such sums were paid beyond the due dates as prescribed under the respective Acts, the right to claim such sums as allowable deduction while computing the income was lost forever.

The assessees' pleas were unsuccessful before the Income-tax Appellate Tribunal. Ultimately, in the case of the impugned judgment, the Gujarat High Court too rejected its pleas.

On appeal, the Supreme Court held as under:

"i) In this scheme the deduction of contributions made by employers to approved provident fund schemes, is the subject matter of section 36(1)(iv). This provision was part of the original Act; it has largely remained unaltered. On the other hand, section 36(1)(va) was specifically inserted by the Finance Act, 1987, with effect from April 1, 1988. The same Act inserted clause (x) to section 2(24) (which defines various kinds of "income"). This is a significant amendment, because Parliament intended that amounts not earned by the assessee, but received by it, whether in the form of deductions, or otherwise, as receipts, were to be treated as income, i. e., amounts received (or deducted from employees) were to be part of the employer-assessee's income. Since these amounts were not receipts that belonged to the assessee, but were held by it, as trustee, as it were, section 36(1)(va) was inserted specifically to ensure that if these receipts were deposited in the employees' provident fund and employees' State insurance accounts of the employees concerned, they could be treated as deductions. Section 36(1)(va) was hedged with the condition that the receipts had to be deposited by the employer, with the Employees' Provident Fund and Employees State Insurance, on or before the due date. The expression "due date" was dealt with in the Explanation as the date by which such amounts had to be credited by the employer, in the concerned enactments such as the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 and the Employees' State Insurance Act, 1948. Such a condition (i. e., depositing the amount on or before the due date) has not been enacted in relation to the employer's contribution (i. e., section 36(1)(iv)).

ii) The Finance Act, 1987 also introduced provisos to section 43B. The intent of the lawmakers was clear that the sum referred to in clause (b) of section 43B, i. e., "sum payable as an employer, by way of contribution" refers to the contribution by the employer. The reference to "due date" in the second proviso to section 43B was to have the same meaning as provided in the Explanation to section 36(1)(va). Parliament therefore, through this amendment, sought to provide for identity in treatment of the two kinds of payments: those made as contributions, by employers, and those amounts credited by employers, into the provident fund account of employees, received from the latter, as their contribution. Both these contributions had to necessarily be made on or before the due date. By amendment of 2003, the second proviso, which mandated that unless the amount of employers' contribution was deposited with the authorities, the deduction otherwise permissible in law, would not be available, was deleted. The court in ***ALOM EXTRUSIONS [2009] 319 ITR 306 (SC)*** was of the opinion that the omission was curative, and that as long as the employer deposited the dues, before filing the return of Income-tax, the deduction was available. The court did not consider sections 2(24)(x) and 36(1)(va) and the separate provisions in section 36(1) for employers' contribution and employees' contribution, went unnoticed.

iii) One of the rules of interpretation of a tax statute is that if a deduction or exemption is available on compliance with certain conditions, the conditions are to be strictly complied with. This rule is in line with the general principle that taxing statutes are to be construed strictly, and that there is no room for equitable considerations. Deductions are to be granted only when the conditions which govern them are strictly complied with.

iv) When Parliament introduced section 43B, what was on the statute book, was only the employer's contribution (section 36(1)(iv)). At that point in time, there was no question of the employee's contribution being considered part of the employer's earning. On application of original principles of law it could have been treated only as receipt not amounting to income. When Parliament introduced the amendments in 1988-89, inserting section 36(1)(va) and simultaneously the second proviso to section 43B, its intention was not to treat the disparate nature of the amounts, similarly. The Memorandum introducing the Finance Bill clearly stated that the provisions – especially the second proviso to section 43B – were introduced to ensure timely payments were made by the employer to the concerned fund and avoid the mischief of employers retaining amounts for long periods. Section 2(24)(x) too, deems the amount received from the employees (whether the amount is received from the employee or by way of deduction authorised by the statute) as income – it is the character of the amount that is important, i. e., not income earned. The significance of this provision is that on the one hand it brought into the fold of "income" amounts that were receipts or deductions from employees income; at the time, payment within the prescribed time – by way of contribution of the employees' share to their credit with the relevant fund is to be treated as deduction [section 36(1)(va)]. This distinction between the employers' contribution [section 36(1)(iv)] and employees' contribution required to be deposited by the employer [section 36(1)(va)] was maintained – and continues to be maintained. On the other hand, section 43B covers all deductions that are permissible as expenditure, or out-goings forming part of the assessee's liability. These include liabilities such as tax liability, cess, duties, etc. or interest liability having regard to the terms of the contract. Thus, timely payment of these alone entitle an assessee to the benefit of deduction from the total income. The essential objective of section 43B is to ensure that even if assessees follow the mercantile method of accounting, the deduction of such liabilities, based only on book entries, would not be given. To pass muster, actual payments were a necessary pre-condition for allowing the expenditure.

v) The distinction between an employer's contribution which is its primary liability under law – in terms of section 36(1)(iv), and its liability to deposit amounts received by it or deducted by it [section 36(1)(va)] is, thus crucial. The former forms part of the employer's income, and the latter retains its character as an income (albeit deemed), by virtue of section

2(24)(x) – unless the conditions spelt out by the Explanation to section 36(1)(va) are satisfied, i.e., depositing such amount received or deducted from the employee on or before the due date. This marked distinction has to be borne while interpreting the obligation of every assessee under section 43B.

vi) The non obstante clause has to be understood in the context of the entire provision of section 43B which is to ensure timely payment before the returns are filed, of certain liabilities which are to be borne by the assessee in the form of tax, interest payment and other statutory liability. In the case of these liabilities, what constitutes the due date is defined by the statute. Nevertheless, assessees are given some leeway in that as long as deposits are made beyond the due date, but before the date of filing of the return, the deduction is allowed. That, however, cannot apply in the case of amounts which are held in trust, as in the case of employees' contributions which are deducted from their income. They are not part of the assessee-employer's income, nor are they heads of deduction per se in the form of statutory pay out. They are others' income, monies, only deemed to be income, with the object of ensuring that they are paid within the due date specified in the particular law. They have to be deposited in terms of such welfare enactments. It is upon deposit, in terms of those enactments and on or before the due dates mandated by such concerned law, that the amount which is otherwise retained, and deemed an income, is treated as a deduction. Thus, it is an essential condition for the deduction that such amounts are deposited on or before the due date. If such interpretation were to be adopted, the non obstante clause under section 43B or anything contained in that provision would not absolve the assessee of its liability to deposit the employee's contribution on or before the due date as a condition for deduction.

vii) In the light of the above reasoning, this court is of the opinion that there is no infirmity in the approach of the impugned judgment. The decisions of the other High Courts, holding to the contrary, do not lay down the correct law. For these reasons, this court does not find any reason to interfere with the impugned judgment. The appeals are accordingly dismissed."

2 *Dy. CGT vs. BPL Ltd.; [2022] 448 ITR 739 (SC): Dated 13/10/2022:*

Gift-tax — Deemed gift — Valuation — Valuation of shares — Gift of shares from promoters' quota during lock-in period — Bar on transfer and no current transactions — Shares not "quoted shares" although companies listed — Valuation to be according to Schedule III to Wealth-tax Act taking restrictions on transfer into account: GTA 1958, Ss. 4(1)(a), 6(1), SCH. II: WTA 1957, Sch. III, Part A, R. 2(9), (11), Part C, RR. 9, 11, Part H, R.21.: A. Y. 1993-94

On March 2, 1993, the assessee gifted 29,46,500 shares and 69,49,900 shares, respectively, in two public limited companies of its group, both listed and quoted on the stock exchange. The shares had been allotted to the assessee on November 17, 1990 and July 10, 1991, and were under a lock-in period up to November 16, 1993 and May 25, 1994, respectively. The Gift-tax Officer concluded

that there was a deemed gift u/s. 4(1)(a) and (b) of the Act to the extent of ₹ 69,78,49,800 and levied gift-tax with interest quantified at ₹ 54,01,12,525.

On appeal the Commissioner (Appeals) ordered tax at ₹ 5.06 crores plus interest at ₹ 7.99 crores. The Tribunal enhanced the tax to ₹ 43.25 crores. On further appeal the High Court held the certificate issued by the stock exchange was conclusive, that there was a lock-in period, that just because the shares were quoted in the stock exchange, that by itself would not mean that some value could be attached, and the value would be so available only if the shares were traded, and that the Commissioner (Appeals)'s valuation was acceptable.

On appeal by the Revenue, the Supreme Court upheld the judgment of the High Court and held as under:

"i) Rules 9 and 11 of Part C of Schedule III to the Wealth-tax Act, 1957 (which, by virtue of Schedule II to the Gift-tax Act, 1958, is applicable to valuation of gifts) relate, respectively, to the valuation of quoted shares and debentures of companies and valuation of unquoted equity shares in companies other than investment companies. The expressions "quoted share" and "quoted debentures", and "unquoted shares" and "unquoted debentures" have been defined in rule 2(9) and (11), respectively, of Part A of Schedule III to the 1957 Act.

ii) When equity shares are in a lock-in period, according to guidelines issued by the Securities and Exchange Board of India, there is a complete bar on their transfer, which is enforced by inscribing the words "not transferable" in the relevant share certificates. While the general circular issued by the Board states that shares under the lock-in period can be transferred inter se the promoters, this would not make them "quoted shares" as defined in rule 2(9) of Part A of Schedule III to the 1957 Act, as the lock-in shares are not quoted in any recognised stock exchange with regularity from time to time, and it is not possible to have quotations based upon current transactions made in the ordinary course of business. Possibility of transfer to promoters by private transfer or sale does not satisfy the conditions to be satisfied to regard the shares as quoted shares.

iii) Rule 11 of Part C of Schedule III to the 1957 Act is a statutory rule which prescribes the method of valuation of "unquoted equity shares" in companies, other than investment companies, which prescription and method of valuation is mandatory in nature. The effect of rule 11 is that unquoted shares must be valued according to the formula prescribed. No other method of valuation is permitted.

iv) Rule 21 of Part H of Schedule III to the 1957 Act is a rule which has been enacted to clarify and remove doubts. Notwithstanding negative covenants prohibiting or restricting transfer, the property should be valued for the purpose of the 1957 and 1958 Acts, but the valuation is not by overlooking or ignoring restrictive conditions. Shares in the lock-in period have market value, which would be the value that they would fetch if sold in the open market. Rule 21 of Part H of Schedule III to the 1957 Act permits valuation of the property even when the right

to transfer the property is forbidden, restricted or contingent. Rule 21, when read carefully, expresses the legislative intent by using the words "hereby declared". Notwithstanding the restrictions, hypothetically the property would be assumed to be saleable, but the valuation in terms of Schedule III to the 1957 Act would be made taking the limitation and restrictions into account, and such valuation would be treated as the market value. Rule 21 permits valuation and ascertainment of the market value in terms of the provisions of Schedule III to the 1957 Act, but does not state that the valuation will be done disregarding the restrictions, or by enhancing the rights which have been transferred, or by revaluation of the asset when the provisions of Schedule III are invoked for the purpose of valuation of an asset under the 1957 Act.

v) However, the certificate from the concerned stock exchange is only to state whether an equity share, preference share or debenture, as the case may be, was quoted with the regularity from time to time and whether the quotations of such shares or debentures are based on current transactions made in the ordinary course of business. The Explanation to rule 2(9) of Part A, Schedule III to the 1957 Act does not prohibit the authority, Tribunal or the court from examining whether a particular share, be it an equity or a preference share, is a "quoted share" or an "unquoted share" in terms of sub-rules (9) and (11) of rule 2 of Part A of Schedule III to the 1957 Act. This right which is conferred on the authorities under the 1957 Act or the 1958 Act is not delegated to the stock exchange. A decision of the authority is amenable and can be examined when challenged in an appeal.

vi) The judgment of the High Court was right."

"It is a tremendous error to feel helpless. Do not seek help from anyone. We are our own help. If we cannot help ourselves, there is none to help us. Thou thyself art thy only friend, thou thyself thy only enemy. There is no other enemy but this self of mine, no other friend by myself."

— *Swami Vivekananda*

"The author of the Mahabharata has not established the necessity of physical warfare; on the contrary he has proved its futility. He has made the victors shed tears of sorrow and repentance, and has left them nothing but a legacy of miseries."

— *Mahatma Gandhi*

Jitendra Singh
Advocate

DIRECT TAXES
High Court

1 ***CIT vs. Raghuraji Devi Foundation Trust [ITXA No. 3 of 2014, order dated 23.08.2022, Allahabad High Court)***

Procedure for registration of Trust or Institution - Section 12AA of the Income Tax Act, 1961 – period of 6 months stipulated in Section 12AA(2) is to be calculated from the date of application made under Section 12AA and any decision taken afresh in pursuance to directions of the appellate authority will not hit by the limitation period of 6 months

Facts

(1) The assessee before the Hon'ble Allahabad High Court had applied for being registered under Section 12AA of the Income-tax Act, 1961 ('the Act') on 05.02.2010 in Form No.10A. Along with the said application, the assessee had also filed an application under Section 80G of the Act.

(2) The Commissioner of Income-tax ('CIT') rejected the application of the assessee on 26.08.2010 by observing that on examination of the evidence on record, it is not possible to arrive at a satisfaction that the assessee is genuinely engaged in charitable activities. The CIT has also rejected the application filed under Section 80G of the Act.

(3) The assessee being aggrieved, preferred an appeal before the Income Tax Appellate Tribunal ('ITAT'). The ITAT vide order dated 12.01.2011 remanded back the matter to the file of CIT for reconsideration.

(4) Pursuant to the order of the ITAT, the CIT reconsidered the applications filed by the assessee. The CIT, however, again rejected the applications of the assessee vide his order dated 23.01.2012.

(5) The assessee, again, being aggrieved by the order of the CIT, challenged the same before the ITAT. The Hon'ble ITAT allowed the appeals vide order dated 20.09.2013 on the ground that once the application of the assessee was not decided within the period of six months stipulated under Section 12AA of the Act after the judgment of

the ITAT dated 12.01.2011, the assessee became entitled for registration under Section 12AA and also approval under Section 80G of the Act.

(6) The department being aggrieved by the order of the appellate tribunal filed an appeal before the Hon'ble Allahabad High Court under section 260A of the Act.

(7) Hon'ble Allahabad High Court, allowed the appeal filed by the department by observing that the application was rejected for the first time within the period of six months as envisaged in sub section (2) of Section 12A of the Act. However, any decision taken afresh, pursuant to the order of the ITAT, would not hit on account of the expiry of the period of six months referred to in Section 12AA of the Act as the said period as is evident from the language used therein is to be calculated from the end of the month in which the 'application was received' which is indicative of the fact that legislature intended that the decision has to be taken before the expiry of six months from the end of the month in which the application mentioned therein was received. The High Court held that it is not the intention that if on an appeal filed against such an order, any directions are issued and thereafter any decision is taken which is taken beyond the period of six months then such a decision would be a nullity in view of subsection (2) of the section 12AA of the Act. Thus, the period of six months referred to in Section 12AA(2) has to be calculated from the end of the months in which the application under Section 12A was received and not from any other date.

2 ***M/s. Bhima Jewellers vs. CIT [ITA No. 15 of 2021, order dated 25.08.2022, Kerala High Court]***

Revision of orders prejudicial to the interest of the revenue - Section 263 of the Income Tax Act, 1961 - CIT revising the assessment order on the ground that for the year under consideration the business loss is not eligible for set off against the income covered under section 115BBE - unjustified. [A.Y. 2013-14]

Facts

(1) During the assessment year 2013-14, the partners of the assessee firm introduced capital amounting to ₹ 3.86 crores. Out of the total capital introduced, an amount of ₹ 1.86 crore was declared as unexplained cash credits under section 68 of the Act into the capital account. The assessee while filing the return of income claimed set off of the business loss of ₹ 1.76 crores against deemed income declared under Section 68 of the Act.

(2) The Assessing Officer ('AO') while finalising the assessment vide order dated 18.03.2016 accepted the capital contribution made by the partners, however, made lumpsum addition of ₹ 3 lakhs to the income already returned.

(3) The CIT issued a notice under section 263 of the Act by observing that unexplained cash credit cannot be treated as business income because it is not an income classifiable under any

head of income as per section 14 of the Act and such incomes are not eligible for set off of brought forward business loss.

(4) In reply to the said notice, the assessee submitted that the unexplained credit into the capital account has been treated as deemed income under Section 68 of the Act. Therefore, it falls under one of the other heads under Section 14 of the Act. Once the deemed income becomes an income earned under one head or the other of Section 14, for the relevant assessment year, there is no prohibition from setting off the business loss from the business income. Thus, the assessment order passed by AO is neither erroneous nor prejudicial to the interest of the revenue warranting interference under section 263 of the Act.

(5) The CIT passed the order under section 263 of the Act by observing that though the submissions made are reasonable and have force, however, the issue is that the AO has not applied his mind to the issue by verifying the facts and therefore the order is erroneous and prejudicial to the interest of revenue.

(6) The assessee being aggrieved by the impugned order challenged the same before the Hon'ble ITAT. The ITAT vide the impugned order dated 20.08.2018 rejected the appeal of the assessee and upheld the order of the CIT.

(7) The assessee being aggrieved by the order of the ITAT preferred an appeal before the Hon'ble Kerala High Court under section 260A of the Act.

Assessee's Submissions before the Hon'ble High Court

(8) The assessee contended before the Hon'ble High Court that the revision order of the CIT suffers from patent illegality as the CIT proceeded on the assumption that deemed income under section 68 of the Act cannot be classified under one head or the other of Section 14 of the Act. Therefore, the set-off should be unavailable.

However, the section as it stood for the applicable assessment year did not have the words "or set off of any loss". Therefore, the insertion to Section 115BBE regulates what can be allowed and what cannot be allowed. As per the applicable section, set off of business loss is not one of the prohibited items for setting off of loss from the income earned by the assessee.

Department's argument before the Hon'ble High Court

(9) On the other hand, the department contended that the order when made by the CIT, the precedent binding on the department was M/s Kerala Sponge Iron Ltd. The CIT has directed re-assessment by following a binding precedent. Hence, the order passed by CIT is valid.

Decision of the Hon'ble High Court

(10) Hon'ble High Court has allowed the appeal of the assessee relying on the decision of the coordinate bench decision in the case of ***Vijaya Hospitality and Resorts Ltd. vs. Commissioner of Income Tax and***

others (2019) 419 ITR 322 and Central Board of Direct Taxes Circular No. 11 of 2019 dated 19.6.2019 wherein it was clarified that since the term 'or set off of any loss' was specifically inserted by the Finance Act 2016, w.e.f. 01.04.2017. Thus, it was held that the assessee is entitled to claim set-off of loss against income determined under Section 115BBE till A.Y. 2016-17.

3 ***Kanakadurga Agro Oil Products Limited vs. ACIT [I.T.T.A. No. 793 of 2006, order dated 26.09.2022, Andhra Pradesh High Court]***

Income derived from an industrial undertaking – Section 80-I of the Income Tax Act, 1961 – Interest received from customers for delay in payments against the sale of goods - interest received having direct nexus with the goods sold – entitled to exemption under section 80-I of the Act. [1997-98]

Facts

(1) The assessee while filing its return of income for the Assessment Year 1997-98 claimed exemption under section 80-I of the Act with respect to the interest received from the debtors, on account of delay in payment of sale proceeds.

(2) The AO, however, while finalizing the assessment order restricted the exemption claimed under section 80-I on the ground that the interest paid was not derived from the business of the manufacture and production of the industrial undertaking.

(3) The assessee being aggrieved by the assessment order preferred an appeal before the Commissioner of Income-tax (Appeals) ['CIT(A)']. The Ld. CIT(A) upheld the view of the AO and denied the exemption claimed under section 80-I of the Act in respect of interest received on account of delayed payment by the customers.

(4) The assessee being aggrieved by the order of the Ld. CIT(A) preferred an appeal before the ITAT. Due to the difference of opinion between the Hon'ble Members of the Appellate Tribunal, the issue was referred for the consideration of Hon'ble Third Members as per the provisions of section 255(4) of the Act.

(5) Hon'ble Third Member opined that the assessee is not entitled to exemption under section 80I of the Act as the interest receivable from the debtors on account of the delayed payments of sale proceeds is not an income derived from the business of industrial undertaking.

(6) The assessee being aggrieved by the order of the Hon'ble ITAT challenged the same before the Hon'ble Andhra Pradesh High Court.

Assessee's Arguments before the Court

(7) The assessee relying on the decisions of the Hon'ble Madras High Court in the case of ***CIT vs. Madras Motors Limited (2002) 122 Taxman 516 (Madras)*** and Hon'ble Gujarat High Court in the case of ***Nirma Industries Ltd vs. CIT (2006) 155 Taxman 330 (Guj)*** contended that the interest received is a direct consequence of the goods supplied. The interest is directly relatable to the amounts received by the assessee during the course of its business on

account of sale to its customers. Thus, the interest income is eligible for exemption under section 80-I of the Act.

Department's Submissions

(8) The department on the other hand contended that the interest paid on delayed payments cannot form part of the same transactions, and as such, it cannot be said that it was a gain derived from its industrial undertaking. Thus, the Hon'ble ITAT was justified in rejecting the claim of the assessee.

Hon'ble High Court's Ruling

(9) Hon'ble High Court allowed the claim of the assessee and rejected the contention of the department by observing that there is direct nexus between the interest received, goods sold and the payments made including interest for the goods sold. It held that the interest received on delayed payments for the goods supplied/sold was profit and gains from business of the same and the same was entitled to relief of exemption under Section 80-I of the Act.

4 ***M/s. Sundaram Finance Ltd. vs. JCIT [T.C.A. Nos. 272 & 275 of 2022, order dated 26.09.2022, Madras High Court]***

Profits chargeable to tax - Section 41(4) of the Income Tax Act, 1961 - Bad debts recovered by the amalgamated company – liable to be taxed under section 41(4) of the Act. [A.Y. 2004-05 & 2005-06]

Facts

(1) The assessee during the assessment years 2004-05 and 2005-06, recovered the bad debts of the companies which got amalgamated into the Assessee, after the amalgamation. However, while filing the returns it has not offered the same for tax on the ground that the said amounts are not taxable in its hands as it is not the 'Assessee' for the purpose of Section 41 of the Act.

(2) The AO however while passing the assessment order held that amounts recovered by the Assessee in respect of bad debt written-off by the amalgamating companies are taxable in the hands of the Assessee.

(3) The assessee being aggrieved carried the matter upto the ITAT. However, the ITAT vide its impugned order upheld the view taken by the lower authorities.

(4) The assessee challenged the order of the Hon'ble ITAT before the Hon'ble Madras High Court under section 260A of the Act.

Assessee's argument before the Court

(5) The assessee, relying upon the decision of Supreme Court in the case of ***Saraswathi Industrial Syndicate Ltd. vs. CIT (1990) 186 ITR 278 (SC)*** and Hon'ble Madras High Court in the case of ***CIT vs. P.K. Kaimal (1980) 4 Taxman 319 (Mad.),*** contended that during the relevant assessment years it recovered the bad debts of the companies, which got amalgamated with it. Hence, the amounts are not taxable in its hands as the assessee is not the 'Assessee' for the purpose under Section 41 of the Act.

Department's argument before the Court

(6) On the other hand, the department contended that the order passed by the Hon'ble Appellate Tribunal is a reasoned one. Thus, no interference is required by this Hon'ble High Court. The department further contended that the decision relied upon by the assessee is prior to the amendment of section 41 and hence, do not apply to the facts of the present case.

Decision of the Hon'ble High Court

(7) Hon'ble High Court upheld the order of the Appellate Tribunal by observing that Section 41 of the Act has to be considered as a complete Code by itself, as far as profit is chargeable to tax. Section 41(1) cannot be read in isolation with Section 41(4). The assessment contemplated under Section 41(1) is the same as the assessment contemplated under Section 41(4). Therefore, merely because there is no corresponding amendment in sub-clause (4), it would not mean that the provisions of Section 41(1) will not apply. Hon'ble High Court further held that the recovery of the debt is a right transferred along with the numerous other rights comprising the subject of the transfer. If the law permits the transferor to treat the whole or part of the debt as irrecoverable and to claim a deduction on that account, it is difficult to accept that the same right should not be recognised in the transferee. Thus, the bad debt recovered by the assessee, which was written off by the amalgamating company, which got amalgamated, is liable to be taxed in the hands of the assessee.

"We read again: "यदिदं किंच जगत् सर्वं प्राण एजति निःसृतम्। -- Everything in this universe has been projected, Prana vibrating." You must mark the word Ejati, because it comes from Eja, to vibrate; Nihsritam, projected;Yadidam Kincha, whatever in this universe."

— *Swami Vivekananda*

"Truth, and nothing but truth is the watchword of the Advaitist. "सत्यमेव जयते नानृतं। सत्येन पन्था विततो देवयान: -- Truth alone triumphs, and not untruth. Through truth alone the way to Devayana lies"

— *Swami Vivekananda*

Neelam Jadhav
Advocate

Tanmay Phadke
Advocate

DIRECT TAXES

Tribunal

1 ***DCIT vs. Shri. Dhaval D. Patel- [ITA No.207/Ahd/2018 dt.10/11/2022 (Ahd) (Trib.) (AY 2013-14)***

Section 23(1)- when the property was vacant throughout the year despite making all possible efforts by assessee, no addition on notional rent can be made and the assessee is entitled to take benefit of Section 23(1)(c)

Facts

The assessee showed the income from properties let out in different years under the head income from house property. However, the Assessee did not show any income in the year under consideration. On the query during the course of the assessment proceeding, the assessee submitted that he could not let out the said properties despite making best efforts and was entitled to claim Sec. 23(1)(c) benefit. The contention was rejected. The assessee filed an appeal before the CIT(A) and succeeded. Thereafter, an appeal was filed before by the Revenue before the ITAT.

Held

The Hon'ble Income Tax appellate Tribunal ["the ITAT" for short] perused the facts and observed that the properties were not let out only for the two assessment years and for the earlier as subsequent years, the same were let out. It was further observed by the ITAT that the assessee took the efforts to the extent possible but could not find out the tenants. The ITAT noted the language of section 23(1)(c) and held that the reasonable construction/interpretation would be that if the property has been let out in any of the previous years, but the same could not be let out despite the best efforts by the assessee in a particular year, the assessee would be entitled to avail the benefits of section 23(1)(c) of the Act. The ITAT also referred to the various decisions of coordinate benches and reached the conclusion that the notional income could not be brought to tax. The ITAT accepted the submissions of the Assessee and dismissed the appeal of the department.

2 *Sai Bhargavanath Infra vs. ACIT [ITA No.1332/PUNE/2019 dt.17/08/2022 (Pune)(Trib.) (AY 2015 – 2016)*

Section 43CA: First proviso is applicable retrospectively and thus where difference recorded between sale value of flats sold by assessee and stamp value of such flats was within 10 per cent margin, no addition to be made to section 43CA

Facts

Assessee was a builder and developer and sold certain flats during the year. During the Assessment Proceedings, the Assessee contended that stamp value was at uniform rate without taking into consideration the peculiar features of a particular property and addition for difference between sale value of flats sold and stamp duty value of the same under section 43CA is not correct. While completing the Assessment the Assessing officer made an addition u/s. 43CA being the difference between sale value of the flats sold and the stamp duty value of the same. The CIT(A) also confirmed the view of the Assessing officer. Aggrieved by the same addition, the Assessee approached to the ITAT.

Held

While deciding the issue the ITAT observed that, the first proviso to section 43CA inserted by Finance Act, 2020 with effect from 1-4-2021 stated that if there was a difference between consideration received by assessee as a result of transfer of land or building and value adopted by Government Authority for purpose of payment of stamp duty was within 10 per cent margin then there could not be any addition on pretext of deemed income. The ITAT considering the Supreme Court decision of ***CIT vs. Vatika Township (P.) Ltd. [2014] 367 ITR 466*** held that if a benefit was provided by Parliament in an existing provision then such an amendment should be given retrospective effect, even without going into merits of case by application of first proviso to section 43CA having retrospective effect. Further held that there is a difference of such value within 10% margin hence there cannot be any addition.

3 *Anant R Gawande vs. ACIT [ITA No.5453/MUM/2019 dt.14/06/2022 (Mum)(Trib.)*

Section 54F: Assessee holding co-owned property cannot be treated as 'absolute owner' while determining claim under section 54F

Facts

The assessee had claimed deduction under section 54F in respect of sale of land against purchase of residential property from India bulls Properties Ltd. Assessee also claimed deduction u/s. 54 on Long Term Capital Gain earned by selling flat. During the course of assessment, AO found that the assessee has purchased one more residential property after investment in property purchased from India bulls Properties Pvt Ltd. The observation of the AO was to avail exemption u/s. 54F the assessee should not own more than one residential house on the date of sale and further assessee should not purchase any other residential house other than the new asset within a period of one year after the date of transfer of the original asset. The AO, observed, the assessee purchased India bulls property jointly along with his

wife, therefore, the assessee was not the full owner of the property which was required by section 54F. The CIT(A) confirmed the view of the Assessing Officer.

Held

The ITAT while deciding the issue observed that, the assessee, was full owner of the first residential property and had 50% share in the second residential property on the date of transfer of original capital asset in the form of a plot. Following decision of ***Amit Gupta vs. ACIT [2017] 43 ITR 427 (Delhi) (Trib.)***, held that the assessee cannot be denied exemption under section 54F merely because he was the holder of 50 % of the share jointly with wife in the the residential property .

4 *Smt. Taraben Jayantilal Patel vs. Dy. CIT, CPC, ITA No.194/AHD./2020 dt. 31/10/2022 (Ahd.)(Trib.)*

Section 143(3) : Assessment - Addition by CPC to be deleted as higher amount of receipts shown in Form 26AS was due to TDS deducted by payers on amount including Service Tax

Facts

The assessee has filed its return of income. The assessee received notice under section 143(1)(a). Further received intimation under Section 143(1) of the Act, where under, the computation of income under the head 'income from house property' was made on a higher side as against returned income as computed by the appellant. A rectification application thereafter was filed by the assessee against the intimation order under Section 143(1) of the Act explaining the reason of difference. The Assessee has computed 'income from house property' excluding of service tax whereas in Form 26AS it is inclusive of service tax. The order upon rectification under Section 154 of the Act, the income under the head 'income from house property' was computed again at higher side instead of as computed by the Assessee. Against the said order, the Assesse filed appeal before the CIT(A). However, the CIT(A) did not accept the explanation rendered by the assessee and confirmed the addition.

Held

The ITAT observed that, the difference pertained to the service tax component as the same was excluded in the income from house property by the assessee but the amount mentioned in Form 26AS was the gross figure inclusive of service tax which was demonstrated /reconciled by the assessee with sufficient evidence. The ITAT deleted the addition as made u/s 143(1) of the Act and allowed the appeal of the Assessee.

"Ignorance is the mother of all the evil and all the misery we see."

— *Swami Vivekananda*

Dr. Sunil Moti Lala
Advocate

INTERNATIONAL TAXATION
Case Law Update

A. HIGH COURT

1 *CIT (IT) vs. Westin Hotel Management - [TS-875-HC-2022 (Delhi)]*

Payments received on account of Centralized Services (w.r.t sales, marketing etc.) do not constitute 'Fees for Technical Services' under the Act as well as the India-US Treaty

Facts

i) Assessee, a US-based company, engaged in the business of providing hotel-related services in several countries including India entered into three agreements with Indian hotels namely, (i) License Agreement for grant of right to use trade name, (ii) Operating Services Agreement and (iii) Centralized Service Agreement.

ii) Amounts received under the License Agreement and Operating Service Agreement being Royalties were offered to tax in India.

iii) Assessee claimed the amount received under the Centralized Service Agreement for providing hotel-related services as business income which was not taxable in India in the absence of a PE. However, the AO held that the services provided by the Assessee were taxable as FTS as per *Explanation* to Section 9(1)(vii).

iv) CIT(A) dismissed the assessee's appeal by holding that the centralized services agreement was merely a subsidiary and ancillary agreement to the main license agreement and would fall within Article 12(4)(a) of India-US DTAA.

v) Further, the Hon'ble Tribunal relied on the jurisdictional HC ruling in the case of Assessee's group entity *viz.* ***Sheraton International [Director of Income Tax vs. Sheraton International Inc (2009) 178 taxman 84 (Del)***] and held that the amount received from customers on account of centralized services viz. sales and marketing, loyalty programs, reservation service, technological service, operational services and training programs did not constitute 'Fee for Technical Service' as defined under Section 9(1)(vii) or Article 12(4)(a) of Indo-US DTAA.

vi) Aggrieved, the Revenue filed an appeal before the Hon'ble High Court wherein the Revenue contended that the judgement of Sheraton was assailed in the Hon'ble Supreme Court and hence was pending adjudication.

Decision

i) The Hon'ble High Court noted that the Revenue had not brought anything on record to distinguish the facts of the present case with the facts of the quoted judgement i.e. Sheraton International which was decided in the favor of the assessee.

ii) It noted that though the said judgement was challenged by the Revenue before the Hon'ble Supreme Court, there was no stay on the said judgement till date.

iii) Further, it relied on SC ruling ***Kunhayammed and Others vs. State of Kerala and Another, (2000) 6 SCC 359*** wherein it was held that mere pendency of SLP does not put in jeopardy the finality of the order sought to be challenged. It was only if the application was allowed and leave to appeal was granted, that the finality of the order under challenge was jeopardised as the pendency of appeal reopens the issues decided and the correctness of the decision could be scrutinised in the exercise of appellate jurisdiction.

iv) It dismissed Revenue's appeal and held that the said income did not constitute FTS and that the judgement of Sheraton International would have a binding effect.

2 *PCIT vs. M/s Boeing India Private Limited- [TS-790- HC - 2022 (Delhi)]*

The Hon'ble Delhi High Court dismissed Revenue's appeal against Boeing India and upheld the ITAT order deleting the disallowance of ₹ 56.58 Cr for non-deduction of tax at source under section 195 of the Act in respect of reimbursement made by it to its AE in respect of payment of salary paid by its AE to the employees seconded to the assessee, and distinguished the co-ordinate bench ruling in Centrica India relied upon by the Revenue

Facts

i) Some expatriates were seconded by overseas entities to its Indian associated enterprise *viz* BICIPL (the assessee) via secondment agreements. The overseas entities paid salary to the seconded employees which were then reimbursed by the Indian Entity. Taxes were duly deducted and deposited under section 192 of the Income-tax Act, 1961 ('Act') on the salary paid to the seconded employees.

ii) The Assessing Officer disallowed the amount reimbursed by the assessee to overseas entities by invoking provisions of section 40(a)(ia) of the Act, on the ground that the Indian entity had failed to deduct tax at source on the amounts reimbursed to the foreign entities.

iii) The DRP upheld the order of the Assessing Officer.

iv) The Hon'ble Tribunal held that the Indian entity (assessee) was the economic employer of the expatriates deputed from overseas entities and noted that the secondees had expressed willingness to be deputed to the Indian entity. Further, it noted that the

Overseas entities agreed to release the employees to the Indian entity and that overseas entities would discharge the salaries to the secondees in the home country on behalf of the Indian entity and that the secondees would work for the Indian entity and would be under supervision, control and management of Indian entity.

v) Further, the Hon'ble Tribunal perused the TDS certificates, Form 15CA and 15CB, tax deducted by the Indian entity and concluded that the Indian entity had deducted tax under section 192. Basis the above, it held that once the tax is withheld under the provisions of section 192, then the provisions of section 195 would not apply. Considering the same, the Hon'ble Tribunal deleted the disallowance made by the AO.

vi) Aggrieved, the Revenue filed an appeal before the Hon'ble High Court.

Decision

i) The Hon'ble High Court noted that the assessee had deducted tax at source under section 192 of the Act and expressed its agreement with the opinion of the Hon'ble Tribunal that section 195 of the Act had no application once the nature of payment was determined as salary and deduction was made under section 192 of the Act.

ii) Further, it distinguished the judgment in Centrica India Offshore Pvt. Ltd (relied on by the Revenue), holding that the said judgement had no application in the present case as the Hon'ble Tribunal had given a finding that the real employer of the seconded employees continued to be the Indian Entity and not the overseas entity.

iii) It further relied on the judgement of the ***Apex Court in DIT(IT) vs. A.P Moller Maersk*** dated 17th February 2017 wherein it was held that "once the character of the payment is found to be in the nature of reimbursement of the expenses, it cannot be income chargeable to tax."

iv) It also relied on the judgement of the Hon'ble Delhi High Court in ***Commissioner of Income Tax Delhi II vs. Karl Storz Endoscopy India (P) Ltd., ITA No. 13/2008 dated 13th September 2010*** wherein it was held that:

'Article 15 states that the salaries, wages and other similar remuneration derived by a resident of a Contracting State (Germany) in respect of an employment shall be taxable in the other Contracting State (India) only if the employment is exercised there i.e. salaries paid to such personnel are taxable in India and not taxable as FTS. Also it added that as per explanation 2 to Section 9(1)(vii) which gives the meaning of the expression FTS as per which inter alia any amount paid as salary cannot be taxed as FTS'

v) Accordingly, it dismissed the Revenue's appeal.

Note:

With respect to the Transfer Pricing Adjustment of ₹ 22.16 lakhs on account of outstanding receivables from Associated Enterprises the Hon'ble Tribunal concluded that no interest was paid to the creditor/ supplier nor any interest had been earned from an unrelated party. Moreover, being a 100% captive service provider, the revenue of the assessee was 100% from its AEs and hence the question of receiving any interest on receivables did not arise. It further relied on

various judgements. The Hon'ble High Court upheld the view of the Tribunal.

B. TRIBUNAL

3 *Trimble Solutions India (P.) Limited vs. ITO [(2022) 141 taxmann.com 331 (Mum- Tribunal]*

Once the margin of profit in the distribution segment had been accepted after consideration of management fees paid, there was no question of making any separate adjustment insofar as payment of management fees was concerned. Accrual of benefit to assessee or commercial expediency of any expenditure could not be a basis for disallowing same

Facts

i) The assessee, an Indian Company was carrying on the business of distribution of software products. It entered into a Distribution Agreement with Tekla Corporation, Finland (associate enterprise) to distribute and sub-license shrink-wrap software products developed by the associated enterprise.

ii) Assessee also entered into a Service Agreement with aforesaid associated enterprise whereby support and guidance were provided to the assessee in the area of marketing, communications, quality management as well as information management services.

iii) In the year under consideration, the assessee had entered into the following transactions with its associated enterprise: a) Purchase of Software Products - ₹ 13,90,61,888 and b) Payment of Management Fees - ₹ 57,97,830. The assessee adopted a combined transaction approach to benchmark the aforesaid international transactions with its associated enterprises using Transactional Net Margin Method ('TNMM') considering the transactions were inextricably linked.

iv) The TPO noted that the assessee had failed to establish rendition, receipt and benefit availed from the services, in respect of which management fees were paid by the assessee to its associated enterprise and treated the arm's length price of international transaction pertaining to 'Payment of Management Fees' as NIL and proposed an upward adjustment of ₹ 57,97,930.

v) The DRP rejected the objections filed by the assessee mentioning that the assessee had failed to satisfy the 'benefits test' and 'willingness to pay test'.

vi) Aggrieved, the assessee filed an appeal before the Hon'ble Tribunal.

Decision

i) The Hon'ble Tribunal observed that the assessee derived various benefits like Quality Management, Corporate Marketing, Information Management, Customer Relationship Management and Corporate Communication, via the agreements entered with the associated enterprise.

ii) It noted the assessee's submission that the managerial service availed from the associated enterprise would not have been able to be performed with the same level of efficiency and effectiveness by a 3rd party vendor given the fact that these services were unique for the group and required expertise and experience in the relevant field and it would have involved very

high cost and also huge amounts in hiring third-party vendors.

iii) It remarked that the TPO neither undertook any benchmarking analysis by adopting any of the prescribed methods under the Act nor searched any comparable transaction for considering the arm's length price at NIL and noted the observations from the judgement of Hon'ble Delhi High Court in ***CIT vs. Cushman and Wakefield (India) (P.) Ltd. [(2014) 46 taxmann.com 317]*** wherein it was held that :

'The TPO's report was binding on the AO subsequent to the Finance Act, 2007. Hence though TPO is empowered to state that the ALP is Nil (after consideration of the facts) given that an independent entity in a comparable transaction would not pay any amount. However, it should not just state that the assessee did not benefit from the said services and hence the expenditure shall be disallowed.'

iv) It further noted that no doubts about payments made by the assessee were raised by the Assessing Officer under section 37 of the Act. Relying on the judgement of the Hon'ble Delhi High Court in the case of ***CIT vs. EKL Appliances Ltd. [(2012) 24 taxmann.com 199***], it held that accrual of benefit to the assessee or the commercial expediency of any expenditure incurred by the assessee could not be the basis for disallowing the same. The Tribunal also relied on the judgements of the Hon'ble Jurisdictional High Court in the case of ***CIT vs. Lever India Exports Ltd. [(2017) 78 taxmann.com 88]*** and that of the co-ordinate bench in the case of ***Hamon Cooling System (P.) Ltd vs. Dy. CIT [(2020) 116 taxmann.com 879]***.

v) It noted that the assessee by considering both the international transactions as inextricably linked had benchmarked them together by adopting the TNMM and that the TPO had accepted the said benchmarking analysis in respect of the international transaction pertaining to 'Purchase of Software Products'. Assessee's margin after considering the expense of management fee was higher as compared to margins of the comparable companies.

vi) It further relied on the judgement of the Hon'ble Delhi High Court in the case of ***Sony Ericsson Mobile Telecommunications India (P). Ltd vs. CIT [(2015) 55 taxmann.com 240]*** and held that once the margin of profit in the distribution segment was accepted after consideration of management fees, then there was no question of making any separate adjustment in so far as payment of management fees was concerned. It thus allowed the assessee's appeal.

4 ***Cadila Healthcare Ltd. vs. DCIT(IT) [(2022) 142 taxmann.com 211 (Ahmdebad-Tribunal]***

Payments made by pharma company in India to non-residents in USA/Canada for clinical trials were held to be not taxable as FTS or royalty and thus were not liable for TDS u/s 195. However, similar payment to a non-resident in Mexico was taxable as FTS in the absence of "make available" clause in the treaty

Facts

i) The assessee, a global pharmaceutical company, had its principal place of business in Ahmedabad, India. With a core competence in the field of

healthcare, the assessee provided healthcare solutions ranging from formulations, active pharmaceutical ingredients and animal healthcare products etc.

ii) During the year under consideration, the assessee made remittances to some non-residents under different heads i.e. to three parties of the USA, one party of Canada and one party of Mexico for clinical trials. Further, one payment was made to one party belonging to the USA towards consultancy fees. No tax was deducted at the source from the said payments.

iii) According to the AO, these remittances made by the assessee to the overseas parties were FTS in nature and thus liable for tax withholding in terms of section 195 of the Income-tax Act, 1961 ('Act').

iv) The CIT(A) allowed relief in respect of payments made for clinical trials to parties in the USA and Canada on the ground that in those cases there was no transfer of any skill or knowledge to the assessee on the issuance of study reports by these overseas entities and hence the "make available" clause in both DTAA's of the USA as well as Canada was not satisfied. The CIT(A) also relied on the Tribunal order in the Assessee's own case for AY 2010-11 wherein the same issue was decided in the favour of the assessee.

v) Regarding the alternate contention raised by the AO, that the said payments would qualify as Royalty, the CIT(A) held that looking into the nature of payments, if the very nature of clinical trials and testing services were considered, it became evident that the services could only come within the meaning of "fee for technical services" and could not be treated as "Royalty". Thus, in respect of payments made towards clinical trials by the assessee to entities situated in the USA and Canada, CIT(A) held that no taxes were required to be withheld.

vi) W.r.t payment made by the assessee to Cambridge and Soft Corporation, USA for consultancy services, the CIT(A) again allowed relief to the assessee on the ground that the "make available" clause was not satisfied in the instant set of facts.

vii) W.r.t to the clinical trial payments to a party situated in Mexico i.e. Ciliantha Research Mexico, amounting to ₹ 90,49,625, the counsel for the assessee submitted before the CIT(A) that it had entered into a supply and distribution agreement with Zydus Pharmaceuticals Mexico, with the objective of promoting its businesses in Mexico. The Assessee argued before the CIT(A) that the case of the assessee was covered under the exception provided in section 9(1)(vii)(b) of the Act read with the clarificatory amendment under Explanation 2, which was to the effect that since the services were both rendered as well as utilised outside India (for the purpose of earning any income from any source outside India), the same was not chargeable to tax in India and hence there was no liability to withhold taxes on these payments. It relied on the judgement of the Hon'ble Delhi High Court in the case of ***DIT vs. Lufthansa Cargo India [60 Taxman.com 187]***.

viii) However, the CIT(A), rejected the plea of the assessee by saying that there is a difference in 'source of income' outside India and 'source of receipt of income' outside India. The

CIT(A) relied on the judgement of ***CIT vs. Havells India Ltd [21 Taxman.com 476 (Delhi)***] wherein it was held that in order to fall within the second exception provided in section 9(1)(vii)(b), the source of income, and not the source of receipt, should be situated outside India i.e. the assessee should have had utilised the services in the business carried on outside India for making or earning income from any source outside India. He added that in this case, the assessee was a mere exporter of products in India and his entire business was situated and carried out in India itself. Hence, he concluded that there was no business outside India and hence exception to section 9(1)(vii)(b) would not be applicable. The CIT(A) also added that since there was no make available clause in the India- Mexico DTAA, such remittance made would be treated as FTS/FIS and thus liable for tax deduction at source.

ix) Aggrieved, both the assessee and the Revenue filed appeals before the Hon'ble Tribunal.

Decision

i) W.r.t to the remittances made to the USA and Canada for clinical trials as well as consultancy, the Hon'ble Tribunal relied on its decision in the assessee's own case i.e. ***ITO vs. Cadila Healthcare Ltd. [(2017) 77 taxmann.com 309 (Ahmedabad - Trib.)]*** and ***ITO v. B.A. Research India (P.) Ltd. [(2016) 70 taxmann.com 325 (Ahmedabad - Trib.)]*** and ***ITO vs. Veedan Clinical Research [144 ITD 297 (Ahmedabad Tribunal)]*** and concluded that the condition of "make available" under the India-USA/India-Canada tax treaty was not being met, and accordingly, the services did not qualify as "fee for technical services/fee for included services".

ii) Further, as to whether these remittances for clinical trials to the USA/Canada could be treated as Royalty, it concluded that the view of the CIT(A) that the remittances made for clinical trials could not be treated as Royalty was correct. It further added that in the instant facts, the payment was towards clinical trials/ testing conducted by an overseas company and they could not be termed as falling under any of the specific clauses of royalty under the India USA/India Canada Tax Treaty. It placed reliance on the judgements of ***Anapharm Inc., In re [2008] 174 Taxman 124 (AAR***) and ***Diamond Services International (P.) Ltd. vs. UOI [2008] 169 Taxman 201 (Bombay)*** and ***Dr. Reddy's Laboratories Ltd. vs. ADIT [2017] 78 taxmann.com 63 (Hyderabad - Trib.)*** to conclude the same.

iii) Accordingly, the Hon'ble Tribunal dismissed the Revenue's appeal.

iv) W.r.t to the clinical trial payments made to the Mexico party, the Hon'ble Tribunal concluded that the said services would qualify as technical services in the absence of the make available clause in the India-Mexico treaty and that thus there was a requirement to deduct tax at source at the time of payment with respect to these services.

v) The Hon'ble Tribunal also rejected the claim of the assessee that the said payment was covered under the exception to section 9(1)(vii)(b) and accordingly dismissed the appeal of the assessee.

CA Naresh Sheth CA Jinesh Shah

INDIRECT TAXES
GST – Recent Judgments and Advance Rulings

A. DECISIONS BY HIGH COURT

1. *GENPACT INDIA PRIVATE LIMITED VS. UNION OF INDIA AND OTHERS [2022-TIOL-1413-HC-P&H-GST] – PUNJAB AND HARYANA HIGH COURT*

Facts and issue involved

Petitioner is engaged in providing following Business Process Outsourcing ('BPO') services remotely through telecommunication and internet link using its own infrastructure and work force:

- Maintaining vendor/customer master data, scanning and processing vendor invoices, book-keeping, preparing/ finalizing books of account, generating ledger reconciliations, managing customer receivables etc.
- Developing, licensing and maintaining software as per clients' needs.
- Technical IT support i.e. trouble-shooting services.
- Data analysis and providing solutions to clients in respect of forecasting of demand for their offerings and management of inventory, supporting various business functions like sourcing and supply chain management.

Petitioner has entered into Master Services Sub-contracting agreement ('MSA') with Genpact International ('GI'), an entity incorporated outside India, to provide BPO services to clients of GI located outside India on principal-to-principal basis.

Petitioner had applied for refund of unutilised ITC for the period of July 2017 to March 2018 which was sanctioned partially by the adjudicating authority. Principal commissioner of CGST Gurugram reviewed the proceedings and passed the order denying export of service benefit on the grounds that petitioner is providing intermediary services. Pursuant to directions of Principal Commissioner of CGST, department preferred an appeal against the refund sanction order passed by the adjudicating authority.

Petitioner has assailed the said order of Principal commissioner under the present writ petition.

Petitioner's submissions

'Intermediary' as defined u/s 2(13) of IGST Act does not include a person who provides services on his own account. Petitioner is rendering services on his own account and is not facilitating supply of services between GI and its customers. Petitioner is responsible for providing all services, for all the risks related to performance of services and pricing. There is no separate agreement entered into between GI's customers and petitioner and therefore in no manner petitioner be equated to an agent of GI. Petitioner is not facilitating supply of services between GI and GI's customer but is actually providing the services 'on his own account' to 'end-customer of GI' on 'sub-contract basis'. Circular No. 159/15/2021-GST dt. 20.09.2021 expressly clarifies that sub-contracting arrangement is not covered under the scope of intermediary as defined u/s 2(13) of IGST Act. Petitioner's turnover includes entire charge for the services (which is the main services) whereas in case of intermediary, turnover comprises of only the commission income.

BPO services rendered by petitioner were held to be export of services under erstwhile service tax regime and refund thereon was regularly sanctioned to the petitioner. Definition of intermediary under service tax regime and GST regime is broadly similar. There being no change in the facts and statutory provisions, appellate authority cannot take a different view. Principle of consistency would apply to tax proceedings.

Revenue's submissions

From perusal of various clauses under MSA it is clear that there are two distinct supplies of services. One, supply of main services (i.e. BPO services) by GI to its customers and second, ancillary support services provided by petitioner. Petitioner is acting on behalf of GI and providing support services so that GI can supply main services to its customers. GI appoints dedicated account representative for each customer who in turn will co-ordinate with petitioner. Such GI representative would have the overall responsibility for managing and coordinating the delivery of services to GI's customers. Such an arrangement where one party (i.e. GI) possesses the authority to take decisions with regard to actions taken by another party (i.e. petitioner) can be referred to as Principal-agent relationship.

Principal of res-judicata does not apply in matters pertaining to tax for different assessment years.

Observations and Discussion by Court

Petitioner is engaged by GI for actual performance of BPO services. Petitioner would be held responsible for all the risk related to performance of services which would be akin to services provided on its own account. Petitioner would share the performance/status of service provision, cost incurred etc. which will enable GI to bill or address any disputes with the customer. Petitioner can access or process the personal data of GI customer to the extent necessary for provision of BPO services. Petitioner would be responsible for maintaining confidentiality of information pertaining to GI customers. MSA also obligates petitioner to provide disaster recovery assistance to GI and also obligates petitioner to maintain records and books in accordance with the law. MSA also lays down manner in which petitioner would raise invoice on GI for the services rendered. If petitioner fails to

perform any obligation under MSA, GI may terminate the contract.

MSA entered between GI and petitioner is clearly for the purpose of sub-contracting services to the petitioner by GI.

Following conditions must be satisfied for a person to qualify as intermediary:

- Relationship between parties must of that of principal-agency;
- Person must be involved in the arrangement or facilitation of provision of service provided to the principal by third party;
- Person must not actually perform the main services intended to be received by service recipient.

Scope of intermediary expressly excludes person who is providing main services on his own account. Various clauses of MSA cannot be interpreted to conclude that petitioner has facilitated the services. The said clauses are in relation to modalities of how the actual work would be carried out and do not in any manner establish that petitioner was required to arrange or facilitate the service between GI and GI customers. Main services were actually rendered by petitioner on his own account.

Order-in-original (for granting refund) passed under service tax regime also recognizes the fact that petitioner provides the main services on its own account. A perusal of definition of intermediary under service tax regime and GST would show that the definition has remained similar. Even the GST circular dt. 20.09.2021 recognizes that definition of intermediary is same in GST and service tax regime. Since there is no change in the definition of 'intermediary', department cannot take different view for different periods. Hon'ble Supreme Court in case of ***Bharat Sanchar Nigam Ltd. vs. Union of India [2006-TIOL-15-SC-ST-LB***] held that where facts and law in a subsequent assessment year are the same, no authority is generally permitted to take a different view.

Pursuant to sub-contracting arrangement, petitioner provides main services directly to overseas customers of GI but does not get remuneration from such customers. It is GI who gets the remuneration for services provided by petitioner. As a sub-contractor, GI receives fees/charges from the main contractor i.e. GI. Nothing has been brought on record to show that petitioner has direct contract with the customers of GI. There is nothing on record to show that petitioner is liaisoning or acting as an intermediary between GI and its customers.

Hence, impugned order holding petitioner to be intermediary cannot sustain.

Decision of High Court

High Court allows the present writ petition.

2. *RSB TRANSMISSIONS INDIA LTD VS. UNION OF INDIA [2022-TIOL-1426-HC-JHARKHAND-GST]*

Facts and issue involved

Department sought to recover interest liability from the petitioner on account of delay in filing GSTR 3B returns. Petitioner denied liability on the ground that amount of tax was already deposited prior to filing of GSTR 3B return in its ECL.

Petitioner challenged the proceedings initiated by department for recovery of interest in the impugned writ petition.

Petitioner's submissions

Interest should be levied only on delayed payment of tax and not on delayed filing of a return as late fees is paid for delayed filing of a return u/s 47 of CGST Act. Section 39(7) of the Act stipulates that the due date of making payment of tax is not later than the last date on which he is required to furnish GSTR 3B return. Thus, the natural inference of the same could be that payment of tax can be made prior to the due date of filing of such return.

Further, on co-joint reading of explanation to Section 49 as well as Rule 87(6) and 87(7), when an amount is deposited towards tax in the Government bank account and is reflected as credited in the Electronic Cash Ledger, upon filing of GSTR 3B return, such amount is merely shown as being debited from the Electronic Cash Ledger and there is no real movement or transfer of money from the petitioner's end as the amount is already in the Government exchequer.

Section 50(1) of CGST Act provides for levy of interest on that part of tax which has been paid beyond the period prescribed. Since the period prescribed for payment of tax is the last date for filing of GSTR 3B return under Section 39(7), interest can only be levied on that part of tax which has been deposited later than the due/last date for filing of GSTR 3B return. The debit entry is only a fictional entry which does not postulate any further movement of money.

Proviso to section 50(1) of CGST Act is to be read in conjunction with basic tenet of levy of interest i.e. compensation for depriving the Government with tax revenue beyond the prescribed time limit.

Observations and Discussion by Court

Combined reading of Sec 39(7), 49(1) & 50(1) of CGST Act along with Rule 87(6) and 87(7) of CGST Rules shows that mere deposit in ECL does not mean that amount is appropriated towards payment of tax. Tax liability gets discharged only upon filing of GSTR 3B return.

Deposits made by challans is reflected in ECL and stays in that ledger till GSTR 3B return is filed. Only then cash ledger is debited and amount is deposited in Government account as tax. Also, registered person can claim refund from balance in ECL after following prescribed procedures under this Act or Rules.

There is a difference between ITC in credit ledger and cash in ECL. Balance available in ECL is deposit, whereas ITC is available to assessee on account of tax already paid. Hence, interest is computed only on amount which is paid by debiting ECL.

The contention of petitioner of having discharged tax liability by mere deposit in ECL prior to due date of filing of GSTR 3B return would be against the scheme of GST Law and make GST Regime unworkable. Revenue has, therefore, rightly computed interest on such delayed payment.

Decision of High Court

The liability to pay interest arises on delayed filing of GSTR-3B return and debit of tax due from the Electronic Cash Ledger. Any deposit in the Electronic Cash Ledger prior to the due date of filing of GSTR 3B return does not amount to discharge of tax liability on the part of the registered person.

B. RULINGS BY APPELLATE AUTHORITY OF ADVANCE RULING

1. *M/s MAHAVIR NAGAR SHIV SHRUSTHI CO-OP HOUSING SOCIETY LIMITED – MAHARASHTRA AAAR [MAH/AAAR/AM-RM/10/2022-23]*

Facts and Issue involved

Appellant is a Co-operative Housing Society registered under Maharashtra Cooperative Societies Act, 1960. Following are the objectives of appellant as per the Society Byelaws:

- To manage. maintain and administer the property of the society.
- To raise funds for achieving the objectives of society.
- To undertake and provide for, on its own account or jointly with a cooperative institution, social, cultural, or recreative activities.

Appellant society raises contributions in the name of "CHARGES". It includes property taxes, water charges, common electricity charges, contributions to repairs and maintenance funds, expenses on repairs and maintenance of the lift, service charges, car parking charges, interest on the defaulted, repayment of the installment of the loan, and interest, non-occupancy charges, etc. Appellant Society does not carry out any other activity other than those mentioned in the bye laws of the society.

Appellant Society has appointed M/s. Unique Rehab Pvt. Ltd. ('contractor') for carrying out major repairs, renovations and rehabilitation works for the society. The said contractor is charging services charges along with GST.

Appellant had sought an advance ruling on the following question:

If the activities of the applicant are treated as "supply" under the CGST Act, 2017 then whether the applicant is eligible to claim the ITC on input and inputs services for repairs, renovations & rehabilitation works carried out by the Applicant?

Maharashtra AAR, vide its order dated 10.11.2021, held that appellant society is not eligible to claim ITC in view of restrictions imposed u/s 17(5) of CGST Act.

Appeal to AAAR and appellant's contentions

Appellant society challenged the above order of AAR on following grounds:

- Appellant society is providing works contract services to its members along with other services i.e. they are receiving works contract services from contractor and in-turn providing such works contract services to members.
- Appellant society shall be eligible to claim ITC of GST charged by contractor as appellant society is providing works contract services to its members. As far as members are concerned, appellant society is the main contractor and M/s. Unique is the sub-contractor. Appellant society is a distinct person from its members and provides works contract services to its members. Hence, ITC should not be blocked u/s 17(5)(c) of CGST Act.
- Section 17(5) of CGST Act contemplates a situation where immovable property constructed is sold post completion resulting into breaking of tax chain. Appellant society is collecting repairs and maintenance charges from members

and GST is paid thereon. Tax chain is not broken in such a scenario. Denial of ITC would be arbitrary, unjust and oppressive.

Discussions by and observations of AAAR

The moot issue is whether appellant society can be construed as providing works contract services to its members.

The main objectives and duties of appellant society as per bye laws is as under:

- To manage. maintain and administer the property of the society.
- To raise funds for achieving the objectives of society.
- To undertake and provide for, on its own account or jointly with a cooperative institution, social, cultural, or recreative activities.

Appellant society is formed with an objective to facilitate or benefit their members by way of undertaking the aforesaid activities. All the activities of appellant society will be covered under heading 9995 having description 'services of membership organization'. Society's core function is to manage, maintain and administer the society property for which it raises required funds from members. Thus, it would be difficult to contend that society undertakes works contract services for their members as repair, renovation, etc. of building would be covered under aforesaid functions of appellant society.

Moreover, appellant society also provides various services such as security services, repair and maintenance services, etc. for which they recover cost from members under 'maintenance charges'. Further, appellant society does not recover cost of such services separately under specified heads. Thus, it is clearly evident that appellant is taking stand of works contract services only to claim ITC which otherwise is not available u/s 17(5)(c) of CGST Act.

Appellant itself is not a works contract service provider nor it is in the business of providing works contract services. The works contract services received by society from appointed contractor is for benefit of all the members. Hence, they are not eligible for the ITC of tax paid to their contractors in terms of the limitations provided under section I7(5)(c) of the CGST Act 2017.

Ruling of AAAR

Appellant society is not eligible to claim ITC of tax paid on works contract services received from contractor.

C. RULINGS BY AUTHORITY OF ADVANCE RULING

1. M/s RITES LIMITED – HARYANA AAR [2022-ARL-19-AAR-GST]

Facts and Issue involved

Applicant is a multi-disciplinary consultancy organization dealing in the field of transport, infrastructure and other related technologies. The nature of various amounts/charges received or forfeited in the course of business are as under:

1. Notice Pay Recovery – This is received in cases where the employee is unable to serve the notice period as per the employment contract.
2. Bond forfeiture of contractual employees – The amount paid as surety is forfeited in case the minimum bond period is not served and the employee resigns before the conclusion of the contract.

3. Canteen Charges – Applicant has entered into a contract with a third-party vendor to provide food and beverages to its employees. Applicant recovers a subsidized amount from its employees for the meals consumed by them and the rest of the amount for the canteen services is borne by the applicant.

4. Recovery on account of loss or replacement of ID Cards – In case of loss or mutilation of existing ID Card, new ID cards need to be made and for the purpose of reissuance, some amount is charged. The printing of the new ID cards and re-issuance is not through any third-party vendor, but through in-house facility itself.

5. Liquidated damages due to delay in completion – Applicant, due to its expertise and being affiliated with Government of India, receives construction work through participating in e-tender. Applicant hires certain contractors to carry out such construction activity. As per the terms of contract between applicant and contractor, if there is a delay in completion of the activity, the contractor is required to pay the agreed sum as liquidated damages.

6. Taxability on forfeiture of earnest money and security deposit and bank guarantee – Applicant receives earnest money deposit (EMD) from bidders, who applies for tender, and returns such money of the unsuccessful bidders except in certain situations.

   Similarly, Security Deposit and Bank Guarantee of the successful bidder may be forfeited in situation where damages may arise.

7. Taxability of amount written off in the books of accounts of the Applicant as creditor's balance – A contractor whose security deposit is forfeited or when such contractor becomes eligible for refund of such deposit but is untraceable and does not come forward to claim such deposit, then said deposit is written off as credit entry in P&L account.

Applicant has sought an advance ruling as to whether:

1. All the above amounts collected/ received by it is liable to GST?

2. If yes, at what rate GST is to be levied?

Applicant's submissions

Applicant submitted as under:

1. Notice period recovery is in lieu of un-served notice period. It does not qualify as 'consideration'. Instead it is compensation received due to breach of the terms of employment contract. Hence, due to absence of any 'consideration' the scope of supply itself is not fulfilled.

2. Canteen services provided by applicant has no nexus with its business and hence, such recovery is not in the course of furtherance of business.

3. Amount recovered on account of loss or replacement of ID Cards is not chargeable to tax as applicant is not in the business of printing ID Cards.

4. Liquidated damages received due to delay in completion of the project is

not taxable as the amount received is not in lieu of any service rendered but is received as damages incurred on account of such delay.

5. Forfeiture of EMD is similar to liquidated damages and hence, such amount is not liable to GST.

6. Creditors balance written off in the books of accounts cannot be treated as amount received for rendering of a service and hence, not liable to GST.

Discussions by and observations of AAR

1. CBIC, *vide* its Circular No. 178/10/2022-GST dated 03.08.2022, has clarified that notice pay recovery and forfeiture of bond surety is in nature of compensation and does not result into the provision of service by either party. Hence, the same is not liable to GST.

2. Applicant is engaged in providing consultancy services and not in catering business. Moreover, Appellate Authority for Advance Ruling, Madhya Pradesh, in a similar matter of M/s Bharat Oman Refineries has ruled that the GST is not applicable on amount recovered from employees towards catering services.

3. Applicant uses in-house printing facility for issuance of ID cards. Amounts recovered for re-issuance of ID cards is not liable to GST as it is covered under Schedule III(1) of CGST Act.

4. Liquidated damages and forfeiture of EMD stands clarified vide Board circular dated 03.08.2022 and hence, it is decided accordingly.

5. Creditor's balance written off does not amount to provision of services and hence, it is not a supply under GST Act.

Ruling of AAR

1. Amount collected by applicant as Notice Pay Recovery from outgoing employees will not be taxable under GST.

2. Amount of Surety Bond forfeited/ encashed by the applicant from outgoing contractual employee would not be taxable under GST.

3. GST would not be payable on subsidized recoveries made by applicant from its employees towards provision of canteen facility.

4. Amount collected by applicant from its employees in lieu of providing a new identity card (ID Card) would not be chargeable to GST.

5. Amount collected by applicant as liquidated damages for non-performance/delay in performance is not taxable under GST.

6. Amount forfeited by applicant pertaining to Earnest Money, Security Deposit & Bank Guarantee due to the reasons mentioned supra would not be chargeable to GST.

7. Amount of creditors balance unclaimed/ untraceable and written off by applicant by way of crediting P&L Account is not taxable.

2. *M/s BAMBINO PASTA FOOD INDUSTRIES PRIVATE LIMITED – TELANAGANA AAR [TSAAR Order No 52/2022]*

Facts and Issues involved

Applicant is a manufacturer of Vermicelli and pasta products. During covid pandemic, applicant had donated oxygen plant to AIIMS hospital Bibinagar, Yadadri Bhongir District, for the benefit of patients who were suffering with low oxygen levels. For this purpose, the applicant has purchased PSA oxygen plant and spare parts for that oxygen plant for Rs. 67,74,200 which includes IGST paid of Rs. 9,16,200. The said expenditure made by them was covered under CSR provisions i.e. Section 135 of the Companies Act, 2013.

Applicant sought an advance ruling as to whether they are eligible to claim ITC on the CSR expenditure incurred by it in accordance with provisions laid down by Companies Act, 2013?

Applicant's submissions

Company is obliged to incur CSR expenditure in order to be compliant with the provisions of Companies Act, 2013 and run its business smoothly. CSR expenditure is an essential part of its business process as a whole.

Section 17(5)(h) of the CGST Act, 2017 blocks input tax credit in respect of "goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples.". A clear distinction needs to be drawn between goods given as 'gift' and those provided/ supplied as a part of CSR activities to satisfy the requirement of law. While the former is voluntary and occasional, the latter is obligatory and regulatory in nature.

CSR expenses incurred by the applicant have been mandated under the Companies Act, 2013. Since CSR expenses are not incurred voluntarily, it doesn't qualify as 'gift' and therefore its credit is not restricted under Section 17(5) of the CGST Act, 2017.

Non-availability of ITC on inputs and input services in case of free supplies of goods/ services shall not be applicable in the present case since the CSR activities, which involves supply of goods or services without any consideration, are said to be done in course and furtherance of business. Therefore, any expense related to CSR activities gets incurred for the purpose of upkeep or running the business.

Uttar Pradesh Advance Ruling Authority in case of Dwarikesh Sugar Industries Limited, has ruled that CSR is a mandatory obligation on a company and hence, expenses incurred by any company in this regard can be considered as incurred in course of furtherance of business. It cannot be considered as gift and hence, ITC is available thereof.

Discussions by and observations of AAR

As per the statutory provisions of the Companies Act, 2013, Companies with a specified net worth or net profit are obliged to incur a minimum of 2 % of their net profit towards their CSR and failure to do so attracts penalty under section 135(7) of the said Act which may go upto a maximum of Rs. 1 crore. Thus, the running of the business of a company will be substantially impaired if they do not incur the said expenditure.

Therefore, the expenditure made towards corporate responsibility u/s 135 of the Companies Act, 2013, is an expenditure made in the furtherance of the business. Hence the tax paid on purchases made to meet the obligations under CSR will be eligible for input tax credit under GST legislation.

Ruling of AAR

Applicant is eligible to claim ITC on such purchases u/s 16(1) of the CGST Act.

3. M/s. ATTICA GOLD PRIVATE LIMITED – KARNATAKA AAR [KAR ADRG 40/2022]

Applicant is engaged in the business of buying and selling second hand gold jewellery i.e. used goods. As majority of purchases are from individuals who are unregistered, applicant has adopted "Marginal Scheme" for discharging their GST liability on sale of such second hand used gold jewellery. Under Marginal Scheme, the value of supply is determined by the difference between the selling price and the purchase price of the goods with a condition that no input tax credit is claimed on purchase of such goods.

Applicant sought an advance ruling in respect of the following questions:

6. Whether applicant, who is under Marginal Scheme, claim input tax credit on the expenses like Rent, Advertisement expenses, Commission, Professional expenses and other like expenses?
7. Whether ITC is allowed to be claimed on Capital Goods under Marginal Scheme?

Applicant's submissions

As a registered dealer, applicant satisfies conditions laid down u/s 16 of CGST Act to claim ITC on any supply of goods or services which are intended to be used in the course of furtherance of his business. Applicant incurs expenses like rent, advertisement, professional expenses, logistics expenses etc. to run the business and without which the business will not run. These expenses are very much required to generate the business and are directly related to their business activities.

Discussions by and observations of AAR

Rule 32(5) of CGST Rules provides that the value of taxable supply, provided by a person dealing in buying and selling of second-hand goods i.e., used goods as such or after such minor processing which does not change the nature of the goods and where no input tax credit has been availed on the purchase of such goods, shall be the difference between the selling price and the purchase price. If the value of such supply is negative, then it shall be ignored.

Rule 32(5) of CGST Rules clearly bars availment of input tax credit on the purchase of those second-hand goods which the second hand goods dealer is supplying. However, there is no restriction on the availment of input tax credit in respect of input services or capital goods.

Further, applicant satisfies all the conditions provided u/s 16 of CGST Act which determines the eligibility and conditions for taking input tax credit.

Thus, there is no bar on the registered taxpayer to claim input tax credit on input services like Rent, Advertisement expenses, commission, professional fees, etc. and also capital goods while being under Margin Scheme [Rule 32(5) of CGST Rules].

Ruling of AAR

Applicant is entitled to claim ITC on input services and capital goods subject to section 16 to 21 of CGST Act and rules 36 to 45 of CGST Rules.

CA Rajiv Luthia CA Keval Shah

INDIRECT TAXES

Service Tax – Case Law Update

1 ***Commissioner of Central Excise and Service Tax, Rajkot, vs. Saurashtra Cricket Association 2022-TIOL-1028-CESTAT-AHM***

Background and Facts of the Case

- The appellants, i.e. M/s. Saurashtra Cricket Association, Rajkot, are engaged in conducting Cricket Matches of International level, National Level and State level at different places in Rajkot Region.
- The respondent is an Association registered under the Society Registration Act, 1860 and had conducted the different Inter District Tournaments matches and BCCI Tournaments Matches during the period from April, 2008 to January, 2009 at various places of Saurashtra-Kutch & Diu as per the direction given by the BCCI.
- It was noticed that the respondent was conducting Cricket Matches as per the direction of BCCI and for that purpose the BCCI are transferring/paying various type of amounts under the cover of subsidies/subvention from the amount of profit which was earned by the by way of conducting matches. It is the contention of the department that the respondent were treated as Sponsor/organizer because they are not organizing the event themselves, but for the same, BCCI has appointed/authorized the respondent to conduct and manage such events.
- The adjudicating authority after considering the submission of the respondent dropped the demand, proposed in the SCN Being aggrieved by the said Order-In-original, revenue filed the present appeal.

Arguments put forth

The Appellants submitted as under:

a. The learned Joint Commissioner (Authorized Representative) appearing on behalf of the revenue reiterates the finding of the impugned order.

The Respondents submitted as under:

b. The Learned CA appearing on behalf of the respondent submitted the details of support from BCCI whereby he has

submitted that the respondent have received subsidy only and not service charges for Event Management Service and respondent have not provided any service to BCCI against the subsidy. He submits that the issue is no longer res integra.

c. The same has been decided in various judgments as follows:-

- ***C. K. Gangadharan-2008 (228) ELT 497 (s.C.) = 2008-TIOL-140-SC-IT-LB***
- ***Priyanka Refineries Ltd.-2010 (249) ELT 70 (Tri. Bang.) = 2009-TIOL-2576-CESTAT-BANG***
- ***Surcoat Paints (P) Ltd-2008 (232) ELT 4 (S.C.) = 2008-TIOL-223-SC-CX***
- ***Board of Control for Cricket in India-2007 (7) STR 384 (Tri. Mumbai) =2007-TIOL-684-CESTAT-MUM***
- ***Vidarbh Cricket Association-2015 (38) STR 99 (Tri.,-Mimbai)= 2013-TIOL-1404-CESTAT-MUM***

Decision

- In the present case the show cause notice was raised by the revenue on the amount receive by the respondent from the BCCI as subsidy. The department has construed the said receipt as service charges received from BCCI against the services of event management. From the facts, it is clear that the respondent have received the subsidy against the expenses incurred for conducting Cricket Matches, therefore, by no stretch of imagination it can be said that the respondent has provided any taxable service to BCCI. This issue has already been considered by this tribunal in the case of VIDARBH CRICKET ASSOCIATION (Supra) wherein the Tribunal has passed the order in favour of the respondents.
- The following subsidies have been given by BCCI - 1) TV Rights subsidy; 2) BCCI tournament receipts; 3) Infrastructure subsidy; 4) BCCI IPL subsidy; 5) Players expenses reimbursements; 6) lease fees for Corporate Box; and 7) subsidy granted by BCCI. The nature of these subsidies needs examination.
- The object of grant of subsiy as evident from BCCI's resolution is —

  (a) to promote the game of cricket in India;

  (b) to arrange, organize, control and finance the visits of Indian Cricket Team to other countries and visits of Cricket Teams of other countries to India;

  (c) to build, construct, maintain and repair various stadia and other amenities;

  (d) to help junior cricketers, needy cricketers, retiring cricketers, players, umpires and other persons connected with the game of cricket;

  (e) creation of infrastructure.
- The question is whether these activities constitute Business Support services as

defined in the law. From the definition of "Business Support Services", it is evident that the support services should be provided in relation to business or commerce. The question is whether conducting cricket tournaments and telecasting the same would constitute business or commerce.

- The Hon'ble Apex Court in the case of Secretary, Ministry of Information and Broadcasting v. Cricket Association of Bengal (supra) held that it clearly comes out that sports organizations are not business or commercial organizations, conduct of sports or sporting events and their broadcasting/telecasting is not assertion of commercial rights.
- The ratio of the above judgment applies squarely to the facts of the case before the judges. It thus clearly emerges that, the service, if at all any, rendered by the appellant is not in relation to any business or commerce and therefore, there is no service tax liability on the said activity under Section 65(104c) read with 65(105)(zzzq) of the Finance Act, 1994.
- In view of the above decision of this Tribunal, it is settled that in the case of the Cricket Association, similarly, placed as the appellant the subsidy received from BCCI was held to be non-taxable. Following the decision in the above case, It was held that the demand in the present case was rightly dropped by the adjudicating authority, Hence, the same is upheld, the Revenue's appeal was dismissed.

2 *Falcon Pumps Pvt Ltd vs. Commissioner of Central Excise and Service Tax, Rajkot 2022-TIOL-1029-CESTAT-AHM*

Background and Facts of the Case

- The appellants have made pre-deposit in terms of Section 35F ibid for admission of the appeal by the Commissioner (Appeals) - The Commissioner (Appeals) also admitted the appeal on payment of 7.5% though the same was paid by way of reversal in the GST-ITC account.
- This clearly shows that the Commissioner (Appeals) has accepted the 7.5% reversal in GST-ITC as pre-deposit in terms of Section 35F. Despite the clear finding, the Commissioner (Appeals) upheld the order-in-original and rejected the appeal for refund of predeposit, which is contrary to own findings, Since the Commissioner (Appeals) agreed that the appellant is eligible to avail the credit in their electronic credit ledger and the appeal for refund of predeposit should not have been rejected. The refund of predeposit should have been allowed if not in cash, but atleast by way of credit in their electronic credit ledger.
- The issue in the present case is that whether the appellant is entitled for refund of pre-deposit made under Section 35F by way of reversal in GST-ITC credit.

Arguments put forth

The Appellants submitted as under:

a. The learned Advocate appearing for the appellant submitted that there is

no dispute that pre-deposit of 7.5% was made for filing of appeal before Commissioner (Appeals) and on succeeding the appeal, the appellant is entitled for the refund of predeposit in terms of Section 35F of Central Excise Act, 1944. Merely because the 7.5% was paid by way of reversal in the GST-ITC account, refund of predeposit cannot be rejected. He placed reliance on the following judgements:

- ***Dell International Services India P. Ltd. 2019 (365) ELT 713 (Tri. Bang.)***
- ***OIO No. 03/REF/2022-23 dated 10.05.2022 (Balson Polyplast Pvt. Ltd.)***

The Respondents submitted as under:

a. The learned AR appearing on behalf of the Revenue reiterates the findings of the impugned order. He submitted that the learned Commissioner (Appeals) has allowed the credit of this pre-deposit amount in their electronic credit ledger, therefore, the appellant should not have any grievance. He also placed reliance on the decision of the Division Bench of Allahabad Tribunal, order dated 23.08.2022, whereby it was held that pre-deposit cannot be made by way of debit in ITC.

Decision

- It was held that there is no dispute that the appellant has made pre-deposit in terms of Section 35F for admission of the appeal by the Commissioner (Appeals). The learned Commissioner (Appeals) also admitted the appeal on payment of 7.5% though the same was reversed in the GST-ITC account. This clearly shows that the Commissioner (Appeals) has accepted the 7.5% reversal in GST-ITC as pre-deposit in terms of Section 35F.
- Despite the above clear finding, the Commissioner (Appeals) has upheld the order-in-original and rejected the appeal for refund of pre deposit which is contrary to his findings. Since the Commissioner (Appeals) has agreed that the appellant is eligible to avail the credit in their electronic credit ledger the appeal for refund of predeposit should not have been rejected, whereas the refund should have been allowed if not in cash, but atleast by way of credit in their electronic credit ledger. This is an apparent error in the order of the Commissioner which needs to be rectified. Accordingly, impugned order is set aside and the matter was remanded to the Commissioner (Appeals) to give a clear order considering his own finding that the appellant is eligible to avail the credit in their electronic credit ledger.

"A perfect life is a contradiction in terms."

— *Swami Vivekananda*

CS Makarand Joshi

CORPORATE LAWS
Case Law Update

Order of Adjudicating Officer of Securities and Exchange Board of India

Name of the Case: In the matter of Bombay Dyeing and Manufacturing Company Limited

Facts of the case

1. Bombay Dyeing and Manufacturing Company Limited (hereinafter referred to as "BDMCL") is part of the Wadia Group of companies and is engaged in the business of real estate, polyester and retail/textile. The equity shares of the company are listed at the Bombay Stock Exchange Ltd. and the National Stock Exchange of India Ltd. The Securities and Exchange Board of India (hereinafter referred to as "SEBI") conducted an investigation to ascertain whether the books of accounts of BDMCL were manipulated for the financial years beginning from FY 2011-12 up to FY 2018-19 (hereinafter referred to as "Investigation Period"/"IP").

2. In FY 2010-11, BDMCL held 49% of the equity share capital of Scal Services Limited (hereinafter referred to as "Scal") and continued to hold the same percentage in FY 2011-12 till March 28, 2012. However, on March 29, 2012, BDMCL sold 30% of its equity share capital in Scal for ₹ 48 Lakhs to Bombay Dyeing Real Estate Company Limited (hereinafter referred to as "BDRECL"), a group company of BDMCL, thereby, bringing down its shareholding in Scal to 19%.

3. During FY 2011-12 to FY 2018-19, BDMCL held 19% of the equity share capital of Scal, the remaining shareholding of Scal was held by other Wadia Group companies namely, Pentafil (19%), BDRECL (19%), Archway (19%) in FY 2013-14), BDS (38% from FY 2014-15), and Springflower (5%). Further on an investigation, it was also found that each of these Wadia Group companies (except Springflower), had cross-holding amongst themselves. For example, in FY 2013-14, the shareholding was as follows:

Shares held by	*Shares held in*		
	Pentafil	*Archway*	*BDRECL*
Scal	25.50%	25.50%	10%
Archway	25.50%	25.50%	10%
BDMCL	49%	49%	40%
Pentafil	-	-	40%

From the shareholding pattern of the said Wadia Group of companies, it was seen that each of these companies was completely held, at any given point in time, in varying proportions, by two or more of the other members of the group. The single common shareholder for these companies, however, at all times throughout the Investigation Period, was BDMCL. Therefore, during the investigation period, BDMCL held the entire share capital of Scal directly as well as indirectly through other group companies. Further, it was alleged that in spite of having significant influence over Scal and having material transactions with Scal, it was not recognised as an 'Associate company' by BDMCL.

4. Further, during the investigation period, the real estate developers, such as BDMCL, were required to recognize revenue from real estate activity in the financial statements in accordance with the "Percentage of Completion Method" as provided in the **Accounting Standard-7** (hereinafter referred to as "AS-7") titled "Construction Contracts". In order to recognise revenue as per AS-7, an entity is required to satisfy the conditions specified in Guidance Note on Recognition of Revenue by Real Estate Developers (hereinafter referred to as "Guidance Note 2006") which are as follows:

   (a) *transfer of all significant risks and rewards of ownership to the buyers;*

   (b) *not unreasonable to expect ultimate collection and*

   (c) *non-existence of significant uncertainty regarding the amount of consideration.*

   In accordance with the same, BDMCL, in its annual reports for every financial year, mentioned that "*the revenue from real estate is recognized on the transfer of all significant risks and rewards of ownership to the buyers*", and further stated that *"it is not unreasonable to expect ultimate collection and that there exists no significant uncertainty regarding the amount of consideration."* ." In order to show that the risks and rewards of ownership have been transferred to the buyers, BDMCL entered into a Memorandum of Understanding (MoU) with Scal for the purchase of flats/ allotment rights in Project One ICC and Project Two ICC, Dadar, Mumbai.

5. The investigation revealed that BDMCL, by entering into various MoUs with

Scal and by subsequently recognizing revenue on the basis of aforesaid MoUs and not consolidating the transactions carried out with Scal, had inflated its sales and profits with respect to its real estate segment during FY 2011-12 to FY 2017-18 to the tune of ₹ 2,492.94 crores and ₹ 1,302.20 crores respectively.

6. Further, during investigation it was submitted by BDMCL, vide letter dated October 17, 2019, that the net amount received till date (October 17, 2019) with respect to MoUs entered into with Scal was ₹ 186 crores which were 7.46% of the revenue recognized by BDMCL during FY 2011-12 to 2017-18 with respect to MoUs entered into with Scal. While the real estate segment's contribution to the total revenue of BDMCL increased significantly in 2 out of 5 years of the Investigation Period, the Real Estate Segment of BDMCL single-handedly contributed to the company's profits during the entire Investigation Period. Even though the 'Polyster' and 'Textile' business segments of BDMCL had volumes in sales but these segments did not translate into profits, rather they incurred losses/ negligible profits during the period under investigation. Further, it was seen that Kalyaniwalla Mistry & LLP, Statutory Auditors of BDMCL during the Investigation Period, had brought to the notice of the shareholders by highlighting this matter under the section "Emphasis of Matter" in their Independent Auditor's report for FY 2014-15.

7. In this regard, SEBI further investigated the role of the then Independent Directors and Chief Financial Officers viz. Mr. R.A. Shah – Independent Director (Noticee no. 1), Mr. S.S. Kelkar - Independent Director (Noticee no. 2), Mr. S. Ragothaman - Independent Director (Noticee no. 3), Mr. S.M. Palia - Independent Director (Noticee no. 4), Mr. Ishaat Hussain - Independent Director (Noticee no. 5), Mr. Raghuraj Balakrishna – Chief Financial Officer (Noticee no. 6), Mr. Vinod Hiran - Chief Financial Officer (Noticee no. 7), Mr. Puspamitra Das - Chief Financial Officer (Noticee no. 8) and Mr. Vishnu Peruvamba - Chief Financial Officer (Noticee no. 9) (collectively referred to as "the Noticees"). On investigation, SEBI alleged that Noticees failed to carry out due diligence even when BDMCL entered into MoUs amounting to Rs 3033 crores. SEBI further alleged that Noticee no.1 to Noticee no. 5 have failed to ensure that the financial reporting process gives true and fair view of financials of BDMCL.

Charge

Noticee nos. 1 to 5 have failed to comply with provisions of Clause 49(II)(D)(1) of the Listing Agreement, Clause 49(III)(D)(1) of the erstwhile Listing Agreement (post amendment dated April 17, 2014) read with Regulation 103 of the SEBI (LODR) Regulations, 2015 and Regulation 18(3) read with Clause A (1) under Part C of Schedule II of SEBI (LODR) Regulations, 2015.

Noticee nos. 6 to 9 respectively have violated Clause 49(V) of the erstwhile Listing Agreement, Clause 49(IX) of the Listing Agreement (post amendment dated 17/04/2014) read with Regulation 103 of the SEBI (LODR) Regulations, 2015 and Regulation 17(8) & 33(2) (a) of the SEBI (LODR) Regulations, 2015

Arguments/submissions by Noticee

1. **SCAL was not an 'Associate Company as per the Companies Act, 2013 and relevant Accounting Standards:** The Noticees submitted that Scal was an associate company till FY 2010-11. After the reduction of stake in Scal to 19% from 49% on March 28, 2012, it was not considered as an associate company for FY 2011-12. Noticees further stated that they have relied on an Opinion dated May 20, 2015, of Manohar Chowdhry & Associates wherein it was stated that BDMCL holds less than 20% of the total share capital in Scal, thus, the requirement to treat Scal as an associate based on the investment criteria is not fulfilled in terms of the first limb of the definition of "associate company" under AS-23. It was also stated therein that Scal does not qualify as an associate of BDMCL under the second limb of the definition of "associate company" i.e. whether the investor exercises control over the business decisions of the investee. The Noticees in their replies also submitted that even as per the Companies Act, 2013, an associate relationship can be established by way of ownership of at least 20% of the total share capital which is not applicable to BDMCL and Scal, as BDMCL throughout the Investigation Period had held less than 20% of the total share capital in Scal. The Noticees have also submitted that BDMCL had no power or control over the business decisions taken by the Board of Scal.

2. **Consolidation of accounts was not required as there was no subsidiary of BDMCL:** In this regard, the Noticees have submitted that Clause 41 of the then Listing Agreement read with Accounting Standard-21 (Consolidated Financial Statements) required a company to provide consolidated financial results only if the company had subsidiaries. Scal was not a subsidiary of BDMCL at the relevant time. Noticees further submitted that compliance with AS-23 is mandatory only if a company prepares consolidated financial statements. As during the FYs 2011-12 to 2013-14, BDMCL did not have any subsidiaries, there was no requirement for preparing consolidated financial statements, and as a result recognition of the effects of the investment in Scal as an associate in the consolidated financial statements did not arise.

3. **SCAL was not considered as Related Party as per the Companies Act, 2013:** The Noticees have submitted that BDMCL and Scal were not related parties under the Companies Act, 2013 for the following reasons:

   a. **Scal and BDMCL** were both **public companies** and **none of the directors** of either of these companies **was a director or held along with his relatives more than 2% of the paid – up share capital** of the other company;

   b. **Neither the Boards** of Directors **nor the Managing Directors** of **BDMCL and Scal** were **accustomed to act** in accordance with the advice, directions or instructions of the other company or any director of the other company. The directors of Scal were self-sustained, with decades of experience in their own right. There is nothing to show that they acted under the control of BDMCL.

c. There was **no holding – subsidiary company relationship** between BDMCL and Scal.

d. Noticees further submitted that an opinion was taken from N. D. Gupta regarding whether Scal can be considered as a related party for Bombay Dyeing or not? On considering these points and Opinion it was decided not to consider Scal as a related party. Noticees further pointed out that during the financial years 2012-13 and 2013-14, BDMCL did not own, directly or indirectly, 20% or more of the voting power in Scal, however, Scal was shown as an associate company purely out of abundant caution, as a consequence of ambiguities in the interpretation of the term after the Companies Act, 2013 came into force, there was no ambiguity that Scal would not be an associate company. Therefore, from FY 2014-15 onward, Scal was referred to as a "group company" for lack of a "better phrase".

4. **Statutory Auditors of BDMCL are left without penalty:** Noticees drew reference to para 11(e) of the Investigation Report whereby SEBI has observed that the auditor's role in directly/indirectly aiding in misrepresentation and non-disclosure of material information in consolidated financials of BDMCL during the Investigation Period has not been established and which is reproduced as under to contend that "Emphasis of Matter" contains a reference to the identified Note to Financial statement and based on the disclosures made in BDMCL's own Financial Statements made by BDMCL. The Noticees have submitted that if SEBI has concluded that BDMCL's statutory auditors had not committed any fraud or misrepresentation or lack of due diligence, SEBI ought to conclude that none of the Noticees can be held guilty of lack of diligence.

Arguments by SEBI

1. **SCAL was not an 'Associate Company' as per the Companies Act, 2013 and relevant Accounting Standards: In this regard** Adjudication officer stated that from **FY 2011-12 to FY 2017-18,** the **total revenue of BDMCL** for the **real estate segment** was ₹ 4,429.57 crores out of which revenue based on MoU with Scal was recorded at ₹ 2,492.94 crores which meant that during FY 2011-12 to FY 2017-18, BDMCL recognized around **56% of real estate revenue based on sales made to Scal**. In fact, during **FY 2013-14**, BDMCL recognised **83% of its revenue from Scal**. Furthermore, the **operating profit** for the real estate segment of BDMCL is ₹ **2317.54 Crores** of which profit before tax on sales made to Scal under the MoUs is ₹ 1302.20 Crores. By emphasising this Adjudication Officer highlighted that BDMCL had material transactions with Scal. SEBI further stated that **Chartered Accountant Firm's Opinion**, wherein it has been stated that Scal cannot be termed as an associate of BDMCL and which has been relied on by the Noticees to show that they have considered expert opinions as members of the Audit Committee, has categorically stated that the **opinion given by them is based on the facts**

and information given to them by BDMCL and that the inaccuracy or incompleteness could have a material impact on the conclusions. SEBI further stated that as per note from page 2 of the Opinion it is seen that BDMCL had submitted to the Chartered Accountant firm that "the transactions between BDMCL and Scal are neither material nor significant during FY 2014 -15". However, I find that BDMCL did **not disclose** to the Chartered Accountant firm that based on the **MoU entered with Scal**, it had recognized revenue of ₹ 301.11 Crores for FY 2014 -15 i.e. the financial year for which the Opinion was provided, which accounted for 68% of the revenue recognized. Based on the above, it is seen that **BDMCL had material transactions with Scal** from FY 2011-12 to FY 2017-18, and **by virtue of the same, BDMCL exercised significant influence over Scal. So the opinion given by** Manohar Chowdhry & Associates **cannot be relied upon as correct facts were not represented to** Manohar Chowdhry & Associates **while giving the opinion. SEBI further highlighted** statements recorded on January 21, 2021, of Mr N H Datanwala that none of the directors of Scal was paid any remuneration. Furthermore, he stated that he is employed with Bombay Burmah Trading Corporation Limited since 1998 and is currently the Chief Financial Officer of the company drawing a salary of ₹ 84 Lakhs per annum. Apart from this, he also receives sitting fees from Macrofil Investments Limited, another Wadia Group company, at the rate of ₹ 3,000/- per meeting. Similarly, Mr. Shailesh Karnik, the then Director of Scal has been drawing remuneration from Nowrosjee Wadia and Sons Limited. Highlighting this SEBI further stated that the **Directors of Scal did not receive any remuneration from Scal**, **nor did they ask for the same**. One of the **most important roles of a director** is to **exercise his independent judgment**. So, SEBI stated that it is **difficult to believe** that the **directors of Scal** who were not drawing remuneration from Scal but from other Wadia Group companies **would exercise independent judgment in the interest of Scal.** This is further corroborated by the fact that the Board of Directors in their meeting held on December 21, 2012, agreed that the sale of the flats held by Scal be executed by BDMCL. **Therefore, it can be seen that BDMCL was exercising significant influence over Scal. Hence, SEBI further stated that by virtue of having material transactions** with Scal and by having representation on the board of directors of Scal, BDMCL **ought to have treated Scal as an 'associate' company and consolidated Scal's financials** in terms of AS-23 read with Section 129 (1) of the Companies Act, 2013 from FY 2014-15 till FY 2016-17, **which it has failed to do which in turn lead to non-compliance with relevant accounting standards and consequent violation of the Listing agreement and LODR Regulations.**

2. **Consolidation of accounts was not required as there was no subsidiary of BDMCL and hence there was no need to consolidate accounts of Scal with BDMCL:** In this regard, SEBI stated that as per Section 212 of the erstwhile Companies Act, 1956 required a holding company to attach to its balance sheet *inter alia* a copy of the

balance sheet of its subsidiary. However, consolidation of financial statements was not mandatory under the erstwhile Companies Act, 1956. On the other hand, under Clause 41(I)(e)(ii) of the erstwhile Listing Agreement, a company having subsidiaries while submitting its annual audited financial results prepared on stand-alone basis was also required to submit annual audited consolidated financial results. Clause 50 of the Listing Agreement required that a company will mandatorily comply with all the Accounting Standards issued by the ICAI from time to time. Therefore, from the above reading of 41(I)(e)(ii) read with Clause 50 of the Erstwhile Listing Agreement, BDMCL would have been required to prepare consolidated financial statements for the FY 2011-12 to FY 2013-14, had they held 50% or more shareholding in Scal or any other company. Further, AS-23, which stipulates criteria for accounting for investment in Associates, would have been applicable to BDMCL, only if the company had prepared consolidated financial statements. However, during the financial years 2011-12, 2013-14 and 2013-14, BDMCL did not have any subsidiary company. Therefore, BDMCL was not required to prepare consolidated financial statements for the financial years 2011-12, 2012-13 and 2013-14. But from FY 2014-15, Archway was shown as a subsidiary by BDMCL. So, BDMCL was required to prepare consolidated accounts from 2014-15. As it was required to prepare consolidated accounts it was also required to comply with AS-23. BDMCL started submitting consolidated financial results w.e.f FY 2014-15 but it did not consolidate accounts of Scal even when Scal was an 'associate' in terms of AS-23/IndAS 28 and BDMCL was required to comply with AS-23/ IndAS 28, by virtue of the mandate under Section 129(1) of the Companies Act, 2013, Clause 50 of the Erstwhile Listing Agreement and Regulation 48 of SEBI (LODR) Regulations, 2015, and therefore, liable for accounting the sales made to Scal and the revenue generated therefrom to the extent of the BDMCL's interest in Scal. BDMCL failed to comply with the stipulations under these Accounting Standards, which would have mandated it to record the investments of BDMCL in Scal under the Equity Method (which would have eliminated the recording of sales of BDMCL to Scal).

3. **SCAL was not considered as Related Party as per the Companies Act, 2013:** As per paragraph 4 of AS-18, an entity with whom the enterprise has a significant volume of business merely by virtue of such economic dependence may not be considered as a "related party". As seen, from FY 2011-12 to 2017-18, the total revenue of BDMCL for the real estate segment was ₹ 4,429.57 crores out of which revenue based on MoU with Scal was recorded at ₹ 2,492.94 crores which meant that during FY 2011-12 to FY 2017-18, BDMCL recognized around 56% of real estate revenue based on sales made to Scal. In fact, during FY 2013-14, BDMCL recognised 83% of its revenue from Scal. Furthermore, the operating profit for the real estate segment of BDMCL is ₹ 2317.54 crores of which profit before tax on sales made to Scal under the MoUs is ₹ 1302.20 Crores. In addition to the significant volume of business between BDMCL

and Scal, BDMCL also held 19% of the shareholding of Scal while the remaining shareholding was held by other Wadia Group companies. Further, it is seen that Scal's office was located in Neville House, J. N. Heredia Marg, Ballard Estate, Mumbai–400 001 which is owned by BDMCL, and Scal did not pay any rent to BDMCL for using the same as office premises. SEBI further noted that the aforesaid facts were overlooked by Mr. N. D. Gupta while stating that BDMCL and Scal were not related parties. Therefore, BDMCL had material transactions with Scal, and by virtue of the same, BDMCL exercised significant influence over Scal for the purpose of AS-18. In view of the above, SEBI stated that BDMCL was exercising significant influence over Scal and therefore, BDMCL ought to have shown Scal as a "related party" for FY 2014-15 in terms of the Erstwhile Listing Agreement (as amended from April 17, 2014) and from FY 2015-16 to FY 2016-17 in terms of SEBI (LODR) Regulations, 2015 read with Clause 50 of the Erstwhile Listing Agreement and Regulation 48 of SEBI (LODR) Regulations, 2015, which it failed to do. SEBI further noted that from FY 2017-18, IndAS became applicable to BDMCL. Thus, it needs to be seen whether Scal was a 'related party' as per Ind AS 24? Para 9(b)(ii) of IndAS 24 identifies an entity being related to a reporting entity if one entity is an associate of another entity. SEBI further noted that the term 'associate' is not defined in IndAS 24, however, Regulation 2(1)(b) of SEBI (LODR) Regulations, 2015 draws the definition of 'associate' from Section 2(6) of Companies Act, 2013. As seen earlier BDMCL held only 19% of the share capital of Scal, and therefore, it did not fall under the definition of 'associate' in terms of Section 2(6) of the Companies Act, 2013. SEBI noted that Scal was not a 'related party' in accordance with IndAS 24 for the FY 2017-18. Thus it is seen that, from FY 2014-15 to FY 2016-17, BDMCL and Scal were "related parties" for the purpose of the Companies Act, 2013 and the LODR Regulations, 2015 which in turn defines "related party" as defined under the Companies Act and the applicable Accounting Standards. Thus, from FY 2014-15 onward, Scal was referred to as a "group company" by BDMCL in its Annual Reports, BDMCL and Scal were related parties and ought to have been disclosed as such in the financial statements of BDMCL. Therefore, it can be concluded that despite being related parties, as shown above, BDMCL failed to comply with the Erstwhile Listing Agreement (as amended from April 17, 2014) and the SEBI (LODR) Regulations, 2015 and the Companies Act, 2013.

4. **Statutory Auditors of BDMCL are left without penalty:** Based on the above analysis, it can be seen that BDMCL ought to have disclosed Scal as an "associate company" and prepared consolidated financial statements from FY 2014-15 which would have eliminated the recording of sales of BDMCL to Scal, which it failed to do. Further, BDMCL also failed to disclose Scal as a related party from FY 2014-15 as was done for FY 2012-13 and FY 2013-14. Further, it needs to be noted that "Emphasis of Matter" is an additional communication in the auditor's report when the auditor considers it necessary to

draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements. By incorporating the section on "Emphasis of Matter", the Statutory Auditors in their limited capacity, highlighted the fact of recognition of sales made to Scal and the corresponding profit recognized. The Noticees were members of the Audit Committee right from the beginning of the Investigation Period and considering the role of the members of the audit committee as stipulated in the Erstwhile Listing Agreement as well as the LODR Regulations. that "Emphasis of Matter" is an additional communication in the auditor's report when the auditor considers it necessary to draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements. By incorporating the section on "Emphasis of Matter", the Statutory Auditors in their limited capacity, highlighted the fact of recognition of sales made to Scal and the corresponding profit recognized. The Noticees were members of the Audit Committee right from the beginning of the Investigation Period and considering the role of the members of the audit committee as stipulated in the Erstwhile Listing Agreement as well as the LODR Regulations, SEBI said that Noticees clearly failed to comply with the applicable provisions of law. Hence the argument that Noticees should be treated on par with the statutory auditors of BDMCL merely because BDMCL had declared Scal as a "group company" and disclosed the revenue recognized by it pursuant to the MoUs entered with Scal was not accepted.

Penalty

Charge against Noticee no.6 is disposed off as he was CFO during the FY 2012-13 and 2013-14 during which consolidation of accounts was not mandatory for BDMCL and also Scal was disclosed as a related party. Penalty is levied under Section 15 HB of SEBI Act, 1992 on Noticees for violating provisions as specified above under the tab 'Charges':

Noticee no.	Name of entity	Penalty
1	Mr R A Shah	10,00,000
2	Mr S S Kelkar	10,00,000
3	Mr S Ragothaman	10,00,000
4	Mr S M Palia	10,00,000
5	Mr Ishaat Hussain	10,00,000
7	Mr Vinod Hiran	200,000
8	Mr Pushpamitra Das	500,000
9	Mr Vishnu Peruvamba	200,000

In the matter of Yadubir Singh Sajwan (Petitioner/Financial Creditor) & Ors. v Som Resorts Private Limited (Respondent/Corporate Debtor) at National Company Law Tribunal (NCLT) New Delhi dated 2nd August 2022

Facts of the Case

- Som Resorts Private Limited (Corporate Debtor/CD) had launched a commercial cum residential project named 'Casa Italia' in 2012 at Ghaziabad, UP. Yadubir Singh Sajwan along with 25 other home buyers (Financial Creditors/FC) had booked space in Casa Italia Project (project) and had made payments to the CD`s agent named Cosmic Structures Limited (Cosmic/Agent) for the booked spaces.

- The FC`s had entered into Builder Buyer Agreement (BBA) with the CD as per which possession was to be handed over in 36 months from the date of commencement of construction.

- However, the CD failed to handover possession of the unit and failed to refund the deposits received from the FC.

- On 11th January 2017 - the Delhi High Court in the winding up petition titled ***Rajni Anad vs. Cosmic Structures Ltd*** had ordered liquidation of Cosmic Structures Limited and the official liquidator had sealed the Project considering the same to be a property of Cosmic.

- The petitioners approached and filed compliant with Economic offence wing against the CD, its promoters and Director. Pursuant to the compliant FIR was registered.

- Thereafter, a Memorandum of Understanding (MOU) was entered between the FC, CD and cosmic on 14th September 2018 to complete the construction of the Project within 18 months of de-sealing of the project sight by Delhi High Court and promised to handover possession to the FC failing which the FC are entitled to get refund of their amount received along with the interest @18% p.a.

- The CD failed to honour its words and defaulted in handing over the possession within the stipulated time frame.

- FC filed a petition u/s 7 of Insolvency and Bankruptcy Code, 2016 (IBC/ code) seeking initiation of Corporate Insolvency Resolution Process (CIRP) against CD for a default of along with interest.

Arguments by the Petitioner

- The CD failed to complete the project within a period of 36 months as stipulated in the Builder Buyer Agreement thereby giving rise of default in terms of section 3(12) of IBC.

- Non-competition of the project has no connection with the submission of allotment documents with CD by the petitioner for two primary reasons —

  — That the project is sealed by UP Awas and Vikas Parishad Construction Division on ground of unauthorised construction against the map approved by the relevant authority

  — The CD has failed to open an escrow account due to its failure to

obtain necessary registration from Real Estate Regulatory Authority.

- If the CD is aggrieved by the breach of MOU/settlement agreement the CD should have initiated necessary proceedings before competent forum

Arguments by the Respondent

- It was submitted that they had entered into a Marketing Agreement with Cosmic solely for the purpose of marketing the Project, against a payment of 10% of the sale consideration amount.
- Allotment Agreements were entered between FC`s and Cosmic directly and accordingly payments were received by the latter without the knowledge of the CD. Hence no debt was due against the CD which it had collected from the homebuyers which led to the difficulties in completion of project.
- Further, submitted that the petitioner had claimed that they had paid an amount of about ₹ 6,60,18,065/- for units of Casa Italia to Cosmic out of which the respondent had received a sum of ₹ 1,45,03,185/- from Cosmic towards the sale consideration which included amount paid by several buyers other than petitioner.
- Cosmic went into winding up proceedings and it was an admitted fact that Cosmic did not release the entire amount to the respondent it had collected for the project 'except to the tune of ₹ 1,45,03,185/-. All these supervening events were not only beyond control of the respondent but outside the knowledge of the respondent which led to the difficulties in the implementation of the project.
- Further, stated that Petitioners were also aware of the illegalities carried out by Cosmic which was entered into a settlement agreement and certain acts were required to be performed by the petitioner and the respondent in seriatum – as in the said case the allotments and agreements were entered into without knowledge or intimation to the respondent and the respondent had agreed to accept the entire money paid by petitioner to Cosmic subject to proof and release from official liquidator.
- Further, e petitioner's association was obliged to provide the copies of allotment agreements and receipts evidencing the proof of allotment to them by Cosmic and proof of payment by them towards the allotment to Cosmic
- In the absence of any payment by petitioner and failure to provide any documentary proof, and due fact that money was yet not released from the official liquidator, the claims of the petitioner were baseless, wilful persistent breach of their obligation.

Held

- It was noted that the CD had given the marketing rights to the Cosmic for a period of one year only, after careful reading of the agreement and examining the nature of relationship between the parties, the agreement was purely an agency agreement wherein the Comic was acting as an agent of the CD.

- Further, highlighted that CD's contention that the allotment agreements were entered between the petitioners and cosmic and the payment were made directly to cosmic without the knowledge or intimation to the CD and accordingly no debt whatsoever was due and payable by the respondent to the petitioner, NCLT was of the view that agreement was executed in relation to the internal affairs of the CD and the petitioners, being outsiders, were not privy to the internal affairs of the CD. The doctrine of indoor management applies here, and therefore, CD cannot be allowed to take advantage of such irregularity at the cost of petitioners.

- Further, the NCLT held that the CD had failed to produce/submit any publication wherein the CD had renounced its association with Cosmic. Therefore, as per the doctrine of indoor management, the petitioners cannot be penalized even if Cosmic was not authorized to execute the Builder Buyer Agreements or to receive the payments for the units allotted in the Project.

- The NCLT highlighted that the 'doctrine of lifting the corporate veil' is an exception to the distinct corporate personality of a company or its members and is well recognized not only to unravel tax evasion but also where protection of public interest is of paramount importance and the corporate entity makes an attempt to evade legal obligations.

- In such circumstances, lifting of veil is necessary to prevent the corporate entities from misusing the principle of distinct corporate personality. It further held that the 'doctrine of lifting the corporate veil' can be invoked, if the public interest so requires or if there is allegation of violation of any law due to the usage of a corporate entity.

- In the present case, the promoter of the CD was also appointed as a director on the board of Cosmic. On lifting the 'corporate veil' of the CD, the NCLT held that the CD and Cosmic were being managed either directly or indirectly by the same person.

- The CD had merely used another corporate entity, i.e., Cosmic to enter BBAs and collect the money from the petitioners with an ulterior motive to conceal the real transaction. Accordingly, it would not be fair to the petitioners, if the CD indirectly achieves its agenda, i.e., to defraud the homebuyers in the disguise of a separate legal entity by concealing the true nature of the transaction.

- Considering the above, the NCLT admitted the petition filed by the petitioners and ordered initiation of CIRP against the CD.

"We reap what we sow We are the makers of our own fate None else has the blame None has the praise."

— *Swami Vivekananda*

CA Hardik Mehta CA Tanvi Vora

OTHER LAWS

FEMA – Update and Analysis

In this article, we have discussed recent amendments made in FEMA through Notifications, Circulars, Press Notes and FAQs.

A. Update through Frequently Asked Questions

1. Annual Return on Foreign Liabilities and Assets (FLA) under FEMA 1999

The FAQs have largely remained the same in comparison to the old FAQs released by RBI on FLA. There are separate FAQs on the FLAIR portal of the RBI which are divided into FAQ 1 and FAQ 2. The following FAQs have been amended/newly inserted in the updated version released on 14th November 2022[1]:

- *Q2. What is the due date of submission of the FLA return?*

  Ans: Entities who comply with the criterion mentioned in Q1 are mandatorily required to submit the FLA return under FEMA 1999 based on audited/unaudited accounts of the entity by July 15 every year.

  (Reference to the specific due date of FLA inserted as a separate question is now inserted. There is no change in the due date but is more clarificatory in nature.)

- *Q13. Is it required to submit Annual Performance Report for ODI if we have submitted FLA Return?*

  Ans: FLA return and Annual Performance Report (APR) for ODI are two different returns and monitored by two different departments of RBI. So, you are required to submit both the returns if these are applicable for your entity. For more information on APR, please refer to the Master Direction – Reporting under Foreign Exchange Management Act, 1999 on RBI's website.

  (RBI has clarified that APR and FLA are different compliances and therefore filing of one does not absolve the requirement of filing the other.)

1. It can be noted that the FAQs on the FLAIR portal have not been updated/replaced. The FAQs 2 on the FLAIR portal mainly deal with section-wise filing assistance of the FLA form and should as such be continued for the purpose of form specific guidance. These have not been merged into the newly released FAQs by RBI. The User manual on "FLA User Registration Form" and User manual on "Filling Online FLA Form" also serve as guidance.

- *Q20. Where should we contact regarding any query/clarification for submission of FLA Return?*

  Ans: Any query regarding filling of FLA return should be sent by email. We will revert back to you within one or two working days.

  (RBI has provided a pathway for solving any queries and clarifications. This process has also been followed in the past through the FLAIR portal but is now inserted via a FAQ)

- *Old FAQ Q 21. What is the system requirement at company's side for filling the FLA Return through web-based online portal?*

  (This FAQ has been merged with FAQ 17 in the updated FAQs)

- *Old Q 22. Where can company/LLP/Others get the format of Annual Return on Foreign Liabilities and Assets (FLA Return)?*

  (This FAQ has been merged with FAQ 17 in the updated FAQs)

- *Old Q 26. Whether equity participation includes equity shares as well as compulsorily convertible debentures (CCD)?*

  (This FAQ seems to have been removed from the updated FAQs. It provided clarity that Compulsorily convertible debentures (CCD) issued by the company should not be included in the paid-up capital while furnishing the information in Paid-up capital (in Section II of the FLA Return). However, if the CCDs/Debentures are held by the non-resident direct investor who is holding the equity shares of Indian reporting company, then CCD/Debentures holding should be reported in 'other capital' component.)

- *Old Q 27. What is Foreign Direct Investment (FDI) in India? viz. Q 28 in the updated FAQs*

  (This FAQ has removed reference to specific section wise guidance on items to be filled into the form as those are included in the user manual and old set of FAQ 2.)

- *Old Q 34. What is Direct Investment abroad by Indian companies? viz. Q 33 in the updated FAQs*

  (This FAQ has removed reference to specific section wise guidance on items to be filled into the form as those are included in the user manual and old set of FAQ 2.)

- *Other capital definition under updated FAQ (Q 24)* has been amended to include : The other capital component (receivables and payables, except equity and participating preference shares investment) of direct investment covers the outstanding liabilities or claims arising due to borrowing and lending of funds, investment in debt securities, trade credits, financial leasing, share application money etc., between direct investors and DIEs and between two DIEs that share the same direct Investor. Non-participating preference shares owned by the direct investor are treated as debt securities & should be included in 'other capital'. Whereas in the old FAQ 1 (Q 30 and Q 36), other capital was explained to include: all other liabilities and claims at Nominal value, except equity and participating preference shares, (i.e. trade credit, loan, debentures, Non-participating share capital, other accounts receivable and payables etc.) of Indian reporting company with non-resident investors.

  (This minor change in explanation of other capital component provides more clarity).

- *Old Q 32. In the FLA Return, whether FDI should be reported based on the country of immediate investor or country of ultimate holding company? Where should we report the receivable/payables with non-resident ultimate holding company?*

  (This FAQ has been removed in the updated FAQs)

- *Old Q 35. If the overseas subsidiaries/ joint venture company's accounting period is different from the reference/ reporting period (i.e. April-March) in the Return, then what information should we furnished in Section IV?*

  (This FAQ has been deleted from updated FAQs since the same answer was already provided in Q 5.)

  (*Source*: FAQs on Annual Return on Foreign Liabilities and Assets (FLA) under FEMA 1999 updated as on November 14, 2022)

B. Modifications in Master Direction

- ***Master Direction – Export of Goods and Services – Modifications made herein give effect to:***

  i) A.P. (DIR Series) Circular No. 09 dated July 08, 2022 on Asian Clearing Union (ACU) Mechanism – Indo-Sri Lanka trade

  ii) A.P. (DIR Series) Circular No. 10 dated July 11, 2022 on International Trade Settlement in Indian Rupees (INR)

  iii) A.P. (DIR Series) Circular No. 13 dated September 28, 2021 on Use of any Alternative reference rate in place of LIBOR for interest payable in respect of export/import transactions

  (Comment: The above circulars have already been covered in detail in the earlier FEMA updates in the August 2022 and October 2021 CTC Journals respectively.)

- ***Master Direction – Master Direction – Import of Goods and Services – Modifications made herein:***

i) Give effect to A.P. (DIR Series) Circular No. 13 dated September 28, 2021 on Use of any Alternative reference rate in place of LIBOR for interest payable in respect of export/import transactions

(Comment: The above circular has already been covered in detail in the earlier FEMA updates in the October 2021 CTC Journal.)

ii) Period for trade credits updated in case of deferred payment arrangements (including suppliers' and buyers' credit) wherein arrangements entered into, for up to three years in case of import of capital goods and up to one year or the operating cycle whichever is less, in case of import of non-capital goods, shall be treated as trade credits. Prior to modification the period for deferred payment arrangements (including suppliers' and buyers' credit) was upto five years for it to be treated as trade credits

iii) The modification to clean credit for import of rough, cut and polished diamonds applies to AD banks requiring them to submit a half yearly report (half year shall be April- September and October-March) of extensions allowed customer-wise, to the respective Regional Office of the RBI within 15 days of the end of the respective half year. Prior to updation the period for which and the time limit within which such report was to be submitted was not provided.

Rahul Hakani
Advocate

Niyati Mankad
Advocate

Best of The Rest

SURENDRA KAPUR VS. M/S PUJA CONSTRUCTION LTD. & 3 ORS – ORDER DATED 03/11/2022 PASSED IN CONSUMER CASE NO. 307 OF 2013 [NCDRC]

Consumer Protection Act, 1986 – Section 2(d)thereof - Complainant being an Investor, therefore, Complaint Not Maintainable

Facts

The Complainant on being approached with respect to a proposed investment opportunity by Opposite Party (**"OP"**), decided to invest an amount of ₹ 17 lakhs initially on the basis of MOU for joint venture project. Subsequently, he invested further amount of ₹ 25 lakhs with letter stating that further amount of ₹ 20 lakhs would be made upon the execution of the Agreement as mentioned in the MOU. However, the builder (opposite party) took a unilateral decision and increased the balance amount that was to be paid and also changed the terms of Agreement. The complainant expressed his disinterest in the project and asked the builder to refund him the money he had already deposited with compound interest.

Following this, the builder entered into a Settlement Agreement dated 21.11.2006 wherein the Complainant was promised a residential duplex flat for his personal use in the Rajmahal Royal Residency Project located in Jaipur. Subsequently, the Complainant and his wife submitted two separate deposit Registration forms along with a cheque of ₹ 10,00,000/- pertaining to two separate flats promised by OP. OP sent letter dated 21.11.2006 to the Complainant acknowledging the entire payment against booking of the said flats and stating that there were no past dues left from either side and full and final receipt of payment for the said flats was confirmed.

However, more than five years had passed (i.e. beyond the deadline set by the parties) and the complainant noticed that no work had been done on the project. The complainant issued a legal notice to OP demanding payment of ₹ 5,00,30,000/-, alleging deficiency in service on the part of the OP. Since, the builder failed to comply with his demands, the Complainant filed the present Complaint u/s 21(a)(1) of the Consumer Protection Act, 1986 (**"said Act"**).

Issues Involved

- That whether the Complainant falls within the purview of the definition of a "consumer"?

- Whether the Opposite Party are liable for breach of contract and deficiency of service?

Held

The Court observed that the Complainant made investment of his money as a partner in the project and now he is seeking refund of that investment amount. The entire transaction between the Complainant and the Opposite Parties was commercial in nature. Refund of the amount sought by the Complainant was only extension of initial investment made by him, which is purely commercial in nature. Moreover, by the Complainant's own admission, *vide* settlement dated 21.11.2016 the said amount was agreed to be 'accounted against' the contractual promise for delivery to the Complainant of a duplex flat. The amount paid along-with accrued interest was the consideration for the flat and the debt was discharged by the OPs through the promise to deliver the duplex flat to the Complainant. Entering into agreement for a duplex flat is only a sequence for realizing the invested amount with interest. Therefore, the Court held that the claim made by the Complainant is only for furtherance of gain for the original investment made. The Complainant being an investor is not a "Consumer" under the provisions of the said Act. The Consumer Complaint was accordingly dismissed, as not maintainable with liberty granted to the Complainant to approach the appropriate Forum.

MRS. MONICA SUNIT UJJAIN VS. SANCHU M. MENON & ORS. – ORDER DATED 02/08/2022 PASSED IN CRIMINAL REVISION APPLICATION NO. 394 OF 2015 [BOMBAY HIGH COURT]

Section 138 of Negotiable Instruments Act, 1881 ("NI Act") - the contract which is forbidden by law is void contract - In cases of money lending business without license (a cognizable offence), the provisions of Section 138 of NI Act are not attracted

Facts

As per the Applicant, she had given a loan of ₹ 12 lakhs to the accused persons in February, 2014. The accused then executed an MoU (Memorandum of understanding) stating they took the money and promised to repay the loan on or before 30.08.2014. The accused then issued five cheques to the applicant but they were dishonored due to 'alteration'. The accused then issued a fresh cheque for ₹ 11.5 lakh. Thereafter, on 02.03.2015, the accused issued a notice admitting to the liability of ₹ 5.5 lakh but in the said notice, the accused mentioned that the said cheques were issued as security to the loan. Cheques were presented by the complainant which was returned with remark "Payment stopped by the drawer". The demand notice dated 17.03.2015 was sent to the accused. The complaint was filed u/s. 138 of the NI Act before the Court of 4th Joint Judicial Magistrate First Class, Vashi at CBD Belapur, Navi Mumbai. The Judicial Magistrate First Class issued process. The accused challenged the order of process by filing a Revision Application before the Sessions Court and the same was allowed. Aggrieved, the Applicant approached the High Court.

Issues Involved

Whether the Session Court erred by setting aside the Order issuing process passed by the JMFC in the facts of the present case?

Held

The court reviewed the sessions judge's ruling and declared that instances of unlicensed money lending businesses are not covered by section 138 of the NI Act. The court inferred from the parties' MoU that the transaction was unlicensed and that the post-dated checks were presented as security. Money lending without license is a cognizable offense. Accordingly, the Court rejected the CRA.

M/S. RAJESHWARA RINGS PRIVATE LIMITED VS. THE ANDHRA PRADESH STATE FINANCIAL CORPORATION – ORDER DATED 22/11/2022 PASSED IN W.P. NO. 4180 OF 2022 [TELANGANA HIGH COURT]

No writ can be issued compelling bank/ financial institution to positively grant the benefit of OTS to a borrower - such a decision should be left to the commercial wisdom of the bank whose amount is involved - It is always to be presumed that that financial institution/bank shall take a prudent decision whether to grant the benefit or not under the OTS scheme

Facts

The Petitioner had availed a term loan of ₹ 336.69 lakhs to set up a unit for manufacture of Precision Engineering Components under General Loan Scheme. The total project was of ₹ 605 lakhs. The said loan was obtained against collateral security worth ₹ 138.02 lakhs by way of urban immovable properties including value of unit's land surplus value of securities offered to the associated unit of the Respondent.

In view of the market situation, the Petitioner decided to close the business by settling all liabilities. The Petitioner approached the Respondent Corporation and made a proposal of One Time Settlement on 18.02.2020. In pursuance of the direction of the Respondents to pay the sum amount for approval under OTS, the Petitioner had paid ₹ 25 lakhs to the Respondent and further paid ₹ 40 lakhs. Even after the payment of total principal amount, the Respondent did not consider the One Time Settlement proposal of the Petitioner and then issued a notice Pro. No. AFC/RRE/MR&R/2021-22/233 dated 30.12.2021 directing the Petitioner to pay ₹ 1,40,73,567/- including O.E.

Accordingly, the Petitioner filed the present Writ Petition seeking writ in the nature of Writ of Mandamus to declare the said Notice dated 30.12.2021 as illegal, arbitrary and consequently, to set aside the same

Issues Involved

Whether writ of mandamus can be issued by the High Court in exercise of powers under Article 226 of the Constitution of India directing a financial institution/bank to positively grant the benefit of OTS to a borrower?

Held

The Court observed that the Petitioner failed to pay the interest and principal amount regularly on the amount obtained to set up the manufacture unit. Relying upon the Supreme Court's Judgment in the case of ***Bijnor Urban Co-operative Bank Limited, Bijnor vs. Meenal Agarwal (2021 SCC OnLine SC 1255)*** wherein it was held that no writ of mandamus can be issued by the High Court in exercise of powers under Article 226 of the Constitution of India, directing a financial institution/bank

to positively grant the benefit of OTS to a borrower and such a decision should be left to the commercial wisdom of the bank whose amount is involved and it is always to be presumed that that financial institution/bank shall take a prudent decision whether to grant the benefit or not under the OTS scheme, the Telangana High Court dismissed the Writ Petition.

MURALI KRISHNA CHAKRALA. VS. THE DEPUTY DIRECTOR, DIRECTORATE OF ENFORCEMENT DATED 23/11/2022 CRI REVISION CASE NO 1354 OF 2022 (MADRAS HIGH COURT).

Prevention of Money Laundering Act – Chartered Accountant cannot be prosecuted for issuing FORM 15CB if documents submitted by client are found ingenuine

Facts

The petitioner (Accused-6 in the original money laundering suit) is a Chartered Accountant who was charged under the PMLA for issuance of Form 15-CB to his client. Form 15-CB is required by banks to send remittances abroad. The petitioner was taken into custody by the Enforcement Directorate (ED) for investigation into a case of money laundering by one of the petitioner's client (Mr. Kiyam Mohammad, Accused-7 in the said suit). The client approached the petitioner for issuance of Form 15-CB for 5 entities. He issued the same to the client without knowing the nature of the business the entities were involved in, the petitioner after verifying the nature of transactions (that the funds had to be transferred abroad) issued certificates for the same under rule 37-BB of the Income Tax Act and also noted that Form 15-CB was not mandatory. The petitioner also uploaded the said certificates to the income tax portal on the same day. The client also furnished the documents of one Mr. Kavin Sidhaarth @ Senthil Kumar (Accused-1 in the original money laundering suit) and on Mr. Kannan (Accused-2 in the said suit) for procuring the Form 15-CB for one of the firms. Later the client did not identify Accused-1 and Accused-2 when he was interrogated by the ED. This led the ED to arrest the petitioner and accused him of being a part of the fraud in the case. The petitioner approached the Madras High Court by the way of this criminal revision petition under Section 397 read with Section 401 of the criminal procedure code.

Issues

1. Whether the petitioner, in his capacity as a Chartered Accountant, was required to inquire into the full nature of business and transactions of the client and the entities seeking issuance of Form-15CB?

2. Should the petitioner have issued the said form without the full knowledge of the persons involved in and running the firms?

3. Whether the Criminal Revision Case filed under Section 397 r/w 401 of the Code of Criminal Procedure should be allowed?

Held

The petitioner submitted that he did not have any reason to suspect the genuineness of the import documents. Therefore, he has neither directly nor indirectly participated in the generation of proceeds of crime in any manner whatsoever. He merely provided 5 certificates of Form-15CB for which he charged ₹ 800-1000 per certificate. It was further contended by the petitioner that Form-15CB was no longer required by nationalised banks for making overseas payments with respect to

imports and if the petitioner had know about the dubious business dealings of his client an if he was a part of the scam then he would not have uploaded the certificates into the Income Tax Department portal on the same day.

The respondent submitted that the petitioner was a Chartered Accountant and as a chartered accountant was free to practise his profession and render professional services in the matter of filing VAT return to the business entity in the name and style of M/s Copy Care, which is owned by A-7 (the client). The Petitioner/A-6, in this case travelled beyond the professional scope, ethics and value and in the process issued the Form-15CB in the name of M/s B.K. Electro Tool Products (one of the five firms which was represented to be owned by A-1 and A-2 by the client).During the interrogation by the ED, the petitioner had then submitted that he had issued a Form-15CB certificate to M/s B.K. Electro Tool Products and also that Form-15CB is required as one of the supporting documents to make foreign remittances. Relying on this and the fact that A-7 has failed to identify the A-1 and A-2 as the owners of M/s B.K. Electro Tool Products, the respondent submitted that the truth can be unravelled only at the time of trial and it is premature at this point of time and for this reason the present petition should not be allowed.

The Madras High Court, in the present petition, held that a Chartered Accountant is not required to go into the genuineness or otherwise of the documents submitted by his clients, his job is to identify the nature of transaction and then issue the Form-15CB that is in question. The court allowed the petition and removed the petitioner as a accused (A-6) in ED's case and held that the petitioner may be called upon to testify as a witness but cannot be an accused in the case.

"We are responsible for what we are, and whatever we wish ourselves to be, we have the power to make ourselves. If what we are now has been the result of our own past actions, it certainly follows that whatever we wish to be in the future can be produced by our present actions; so we have to know how to act."

— *Swami Vivekananda*

"Man often becomes what he believes himself to be. If I keep on saying to myself that I cannot do a certain thing, it is possible that I may end by really becoming incapable of doing it. On the contrary, if I have the belief that I can do it, I shall surely acquire the capacity to do it even if I may not have it at the beginning"

— *Mahatma Gandhi*

CA Vijay Bhatt
Hon. Jt. Secretary

CA Mehul Sheth
Hon. Jt. Secretary

THE CHAMBER NEWS

Important events and happenings that took place online/ physical between **1st November, 2022 to 30th November, 2022** are being reported as under:

I. ADMISSION OF NEW MEMBERS

The details of new members who were admitted in the Managing Council Meeting held on 18th November, 2022 are as under:

Type of Membership	No. of Members
Life Member	14
Ordinary Member	01
Half Yearly Ordinary Member	18
Student Member	05
Total	**38**

II. PAST PROGRAMMES

<table>
<tr><th>Sr. No.</th><th>Date</th><th>Topic</th><th>Speaker</th></tr>
<tr><td colspan="4">COMMERCIAL & ALLIED LAWS</td></tr>
<tr><td>1.</td><td colspan="3">The Commercial & Allied Laws Committee had planned a Virtual program on “2-day online course on Black Money and Benami Act” The session-wise details for the program is as under:</td></tr>
<tr><td>a.</td><td rowspan="2">04.11.2022</td><td>Incisive Analysis of Key Definitions, Charge of Tax and Scope and Computation under the Black Money Act</td><td>CA Pradip Kapasi</td></tr>
<tr><td>b.</td><td>Penalties and Prosecution under Black Money Act</td><td>V. Shridharan,
Senior Advocate</td></tr>
</table>

Sr. No.	Date	Topic	Speaker
c.	05.11.2022	Key Definitions and Prohibition of Benami Transactions, Relevance with Trust Law and Case Studies	Vipul Joshi, *Advocate*
d.		Attachment of Properties and Adjudication under the Benami Act	Devendra Jain, *Advocate*
e.		Panel discussion on Interplay between Black Money Act, Benami, PMLA and Income-tax Act	CA Pradip Kapasi & V. Sridharan, *Senior Advocate*
DIRECT TAXES			
1.	04.11.2022	Recent Important Decisions under Direct Tax	CA Nikhil Tiwari
2.	08.11.2022	Lecture Meeting on recent decisions of Supreme Court on taxation of Charitable Institutions	CA Gautam Nayak
3.	The Direct Taxes Committee had planned a Virtual program on "Full Day Webinar on Landmark Income-tax Rulings" The session-wise details for the program is as under:		
a.	12.11.2022	Keynote Address	Hon'ble Justice Shri K. R. Shriram (Sitting Judge Bombay High Court)
b.		Constitutional Validity and Scope of Income	Saurabh Soparkar, *Senior Advocate*
c.		Computation of Income – salary, business income (28, 37(1)), capital gain, IOS, etc	Ajay Vohra, *Senior Advocate*
d.		Tax Proceedings – Assessment, Reassessment, CIT(A), 263, 264, ITAT	*Hiro Rai, Advocate*
e.		TDS, Tax Demand, Interest and Refund	Nitesh Joshi, *Advocate*
f.		Penalty and Prosecution	V. Shridharan, *Senior Advocate*
INDIRECT TAXES			
1.	16.11.2022	Intricate Issues in filing of GSTR-9 and GSTR-9C	Chairman - CA Vikram Mehta Group Leader - CA Archit Agarwal
STUDY CIRCLE & STUDY GROUP			
1.	15.11.2022	Taxation of Shares & Securities	CA Jignesh Shah

International Taxation Committee

1st Residential Refresher Conference on the Foreign Exchange Management Act 1999 and its Rules/ Regulations (with focus on practical aspects) held from Friday, 2nd to Sunday, 4th December, 2022 at Hilton Garden Inn, Pune.

Brain Trust Session

Moderator: CA Manoj Shah, *Panellists* : CA Dhishat Mehta & CA Shabbir Motorwala addressing the delegates

Group Photo

Pre-Budget Memorandum 2023-2024

CA Parag Ved (President), CA Mahendra Sanghvi (Chairman - Law & Representation Committee) and CA Ketan Vajani (Co-Chairman - Law & Representation Committee) submitted the physical Pre-Budget Memorandum 2023-2024 to Shri Nitin Gupta, Chairman CBDT, Delhi on 23rd November, 2022.

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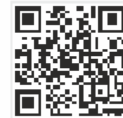

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