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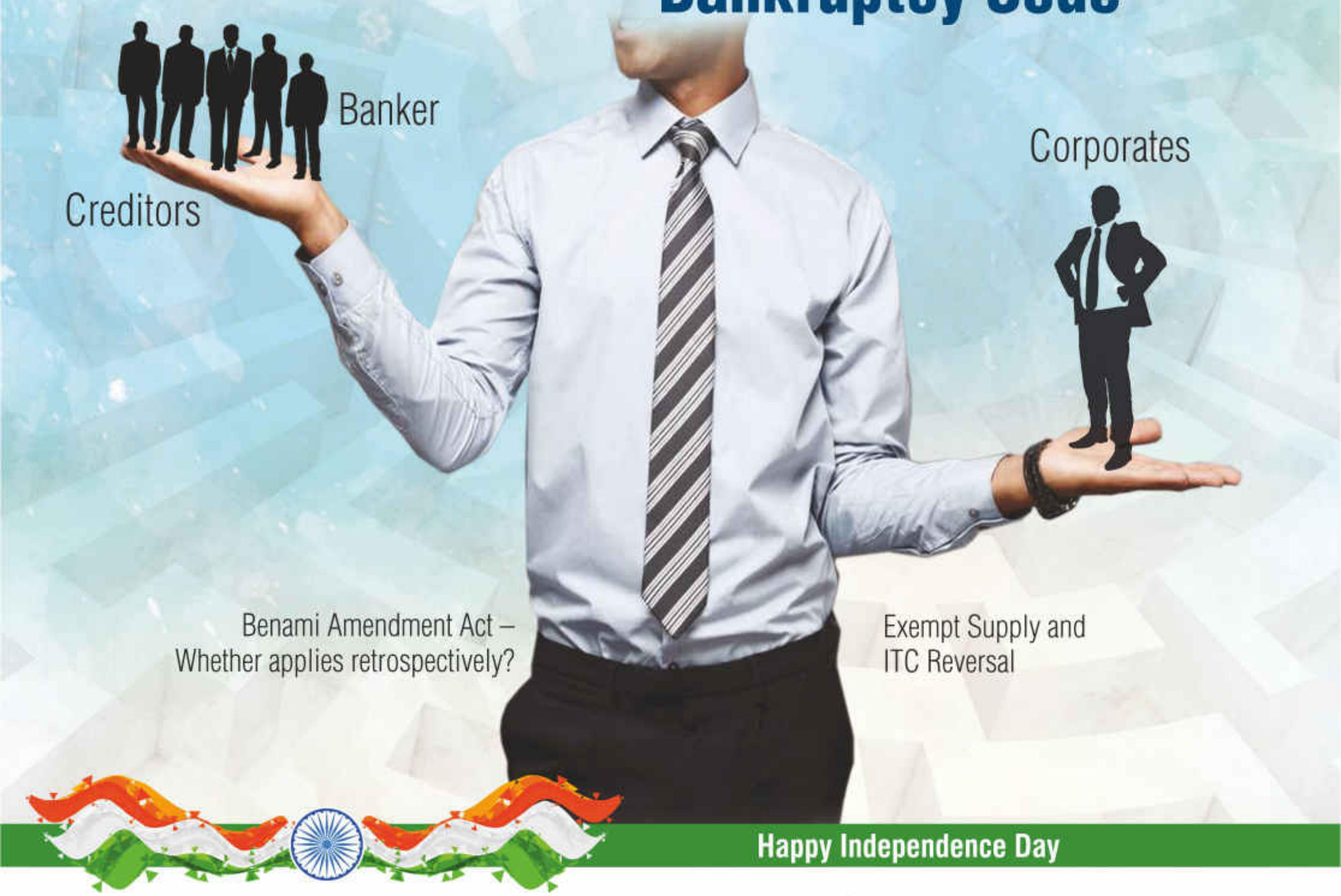
THE CHAMBER'S JOURNAL

Vol. VII | No. 11
August 2019

Your Monthly Companion on Tax & Allied Subjects

Insolvency and Bankruptcy Code



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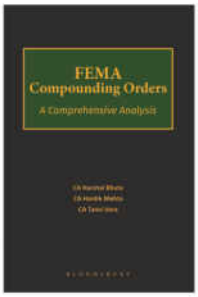

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Editorial

TAX ………… TERRORISM ………. TAXORISM

When I pen down this editorial, the phrase that has become the flavour of the season is "Tax Terrorism" ["TT"]. So much intense passion this phrase has generated on account of the suicide of V. G. Siddhartha, the founder of CCD – with the opportunists, as usual, merrily joining the bandwagon – that within the Editorial Team there was even discussion to incorporate a couple of articles, if not a special story, on this 'hot' topic.

This is typical of Indian mass psychology/mass response/mass behaviour/mass reaction. A knee-jerk reaction, generated out of mass hysteria, is always counter-productive. Such type of reaction that is merely a symbolic/token has always a short shelf-life. The mood whittles away/evaporates soon, until another more shocking [read "juicy"] story is churned out. Such phenomenon is popularly attributed to the age old wisdom: *"The public memory is too short"*.

Given the fact that India had one of the finest pasts in the world with a glorious ancient civilization so rich in all fronts, it is quite amazing how the glory has faded into oblivion, with India now ranking far behind in almost all significant spheres of human life index and the countries with no glorious past but of recent origin having marched past India having gone far ahead. While this may be an interesting topic for discussion/debate, what is sought to be highlighted here is a very peculiar attribute – which is certainly not something to boast about.

Today, the great Indian mass psychology suffers from two extreme attributes. One, extreme tolerance to all the senseless that is going around; be it on political front, on environment front, on economic front, on civic sense front, on corruption front, on education front………the list is truly endless! The public at large has become too indifferent to the wrong things happening around. A state of affairs or an event which otherwise would shake the conscience of citizens of any civilized world, can pass through this sub-continent unnoticed or, if noticed, would go unchallenged without much eyebrows being raised. The recent event of the ghastly attack on the Unnao rape victim and his family/lawyer is one such latest shameless episode! Either the spirit has been drained out completely on account of extreme adverse economic or other factors or such indifference/tolerance has become an integrated part of routine nature of citizens, who are still in deep slumber basking in the glory of their ancient past! At this juncture, it may be apt to reproduce an extract from the Preface penned by our beloved Shri Nani Palkhivala for the 8th Edition of his treatise "*The Law and Practice of Income Tax"*, a reference to which was made in my last Editorial. {Mind you, these were in the context of Indian tax laws!}

> *"G. K. Chesterton, in his brilliant essay 'The Mad Official', analyses how a society goes mad. The rot begins, he says, when wild actions are received calmly by society. 'These are people that have lost the power of astonishment at their own actions. When they give birth to a fantastic passion or foolish law, they do not start*

or stare at the monster they have brought forth… These nations are really in danger of going off their heads en masse, of becoming one vast vision of imbecility.' India is one such country in respect of budgeting and fiscal laws. Today, the monster of our direct tax structure has become more monstrous than ever before.

Two things strike the student of Indian income-tax law with trepidation and amazement – the precipitate and chronic tinkering with the law by bureaucrats who are the unacknowledged legislators of India, and the anaesthetized patience of the Indian public. Truly, we Indians are a 'low arousal' people. We endure injustice and unfairness with feudalistic servility and fatalistic resignation. The poor of India endure inhuman conditions which would lead to a bloody revolution in any other country. The rich endure foolish laws and maddening amendments which benefit none except the legal and accountancy professions, and instinctively prefer to circumvent the law than to fight for its repeal."

We have tolerated so much for so long time that we have become immune or shock proof to what is going on around us. Nothing surprises us, nothing affects us, nothing bothers us and nothing provokes us………….. The tax regime is one such aspect.

At the other end is the tendency to give extreme reaction to an event, at a slightest of provocation. Here, the situation is reverse. A state of affairs or an event which would pass smoothly, unnoticed and without being bothered about in most of the civilized world becomes not only a matter of great debate at length but evokes extreme reaction, most of the times culminating in violence and acquiring political colour. A totally insignificant or irrelevant event consumes the nation's passion, peace and the limited resources – in terms of waste of public property, public time, public exchequer – coupled with putting great strain on government and enforcement agencies' machineries as well as on the judiciary. ……….The tax regime is one such aspect.

From the prism of the civilized world, such extreme and paradoxical behaviour can be too baffling, if not too disturbing.

The recent controversy involving the tax regime on account of the suicide of V. G. Siddhartha is a classic example of such extreme behaviour/reaction, with the widely circulated video clip of Mr. Mohandas Pai, Ex-Director/CFO of Infosys, in the social media igniting the debate, some observations of which are difficult to appreciate, especially in absence of proper knowledge about the factual and legal background of the case. And then, of course, there is also the other side of this fear-mongering.

{P.S.: The above editorial was penned on 3rd August. On 4th came the news about the President of India's Notification – "Presidential Order" – about Jammu & Kashmir and Ladakh! The entire nation got immersed, first with shock and awe and then with heated discussions across all forums of social interaction. And so did the then 'live' issue of 'tax terrorism" quietly and quickly get out of public mind and sight! Just like that! The entire topic of TT, so live and hot up to 4th August, now looks ghostly and pertaining to distant past! Did I say earlier, public memory is too short? I don't recollect now!!}

Vipul B. Joshi
Editor

From the President

Dear Members,

On the eve of India's 73rd Independence Day, the Government took a momentous decision by abating Article 370 of the Constitution and superseding Article 35A, thereby effectively ending Jammu and Kashmir's special status. This means that the Constitution of India will now apply in full force across Jammu & Kashmir (J&K) and Ladakh, which will now be two separate Union Territories. People of other states will now be eligible to purchase land and properties. No- permanent residents can permanently settle in these territories and outsiders can now be employed in State Government services and companies. J&K which, despite it being a favoured tourist destination, has remained economically backward for several decades due to various reasons will hopefully now see further economic development. The Government has received appreciation from all corners of the society for its bold decision in the overall interest of the country.

While the country is rejoicing on this momentous occasion, the country has lost one of the most revered, respected and loved politicians, Smt Sushma Swaraj. She was a strong and fearless leader, an orator par excellence and one of the most outstanding politicians in the present era. She was an epitome of dignity in all the positions she held. Very few politicians of today can command the respect which she did. India truly has lost a tall leader who made significant contribution as a Parliamentarian who would be fondly remembered for many years.

Another development which has made all the countrymen proud is the launching of Chandrayaan-2 on 22nd July 2019 by the Indian Space Research Organization (ISRO). It consists of a lunar orbiter, a lander, and a lunar rover named Pragyan, all of which have been developed in India. The main scientific objective of launching Chandrayaan-2 is to map the location and abundance of lunar water. The lander and the rover will land on the rear side of the Moon, in the south polar region, on 7 September 2019. A successful landing would make India the fourth country to achieve a soft landing on the Moon, after the USSR, USA and China. This is indeed a matter of pride for all of us!

While there have been positive developments in the overall interest of the country, the economic scenario, on the other hand, sadly does not look over encouraging and the overall sentiments are weak and gloomy. The Budget 2019 presented by the Honble Finance Minister has not been received well by the people at large and therefore the Stock Market has nosedived eroding a huge amount of wealth of investors. The fall after this year's budget has been unprecedented. One of the major causes of this fall is the levy of the increased surcharge on non-corporate Foreign Portfolio Investors.

Needless to mention that overall weak economic scenario is also one of the reasons for this fall. The Government should take immediate measures to revive the economy. Another point worth mentioning here is that the Government was in the unnecessary haste in passing the Finance Bill (No2), 2019 without giving adequate opportunity to the stakeholders to make their representations. This is least expected from the present Government.

The recent Monetary Policy of the Reserve Bank of India declared on 7th August 2019 appears to be a step to revive the economy. For the fourth straight time in a row, the RBI has cut its benchmark repo rate by 35 basis points. The higher than expected rate cut of 35 basis points clearly shows the RBI's concern about the present less than ideal performance and uncertain outlook, on the back of diminishing growth and the urgency to take measures to fuel growth.

One of the noteworthy feature of this policy is that RBI will soon issue detailed guidelines on permitting banks to on-lend through NBFCs. This is being done to increase credit flow to certain priority sectors which contribute significantly to the economic growth in terms of export and employment.

While the recent monetary policy is a step to revive the economy, the Government is serious about amending the existing statutes and enacting new laws with a view to curb regulatory gaps, making statutes administratively strong and in some cases making them more practicable like in the case of Bankruptcy Code.

The Bankruptcy Code was enacted in December 2016, largely with a view to address the problem of resolution of NPAs. The Code has helped in addressing the issue to some extent but there were a lot of practical difficulties in implementing and therefore much needed amendments have been brought out in the Code which would hopefully result into more resolutions than liquidations.

In its endeavour to save gullible investors from Ponzi schemes, the Union Cabinet has approved Banning of Unregulated Deposit Schemes Bill. The bill will replace the banning of Unregulated Deposit Schemes Ordinance, 2019. The Bill will help tackle the menace of illicit deposit taking activities in the country, which at present are exploiting regulatory gaps and lack of strict administrative measures to dupe poor and gullible people of their hard-earned savings.

There are some significant amendments under the Companies (Amendment) Act, 2019 Some of them are a further step to promote ease of doing business, mandatory spend towards CSR, more accountability and improved enforcement to strengthen corporate governance norms etc.

The month of July witnessed some of the exciting sports events as well. The Cricket World Cup final between New Zealand and England were one of the best cricket matches one would have ever witnessed. The way the result of the match was decided also generated lot of debate and discussion Though England was the winner of the World Cup, for all practical purposes, both the teams were the winners. In the excitement of the Cricket World Cup, the remarkable feat of the Indian sprinter, Hima Das did not get as much attention as it ought to have. She won five gold medals in less than three weeks which is indeed a rare feat and she has truly made our Country proud.

REPRESENTATIONS

The Chamber is always at the forefront in making representations to various Government authorities such as CBDT, GST Council, MCA, SEBI and other authorities.

1. In line with the above, we made representation to the CBDT for extension of the Income Tax return filing due date for A.Y. 2019-20 due to hardship faced by the tax payers as well as professionals. Much to the relief of the taxpayers and professionals, the extension has been granted till 31st August.

2. A separate representation was also made to CBDT suggesting changes in various Tax Returns for A.Y. 2019-20 and issues relating thereto.

Representation was also made to GST Council for changes in the GST Act and Rules.

A representation was made to the Women & Child Development Department for extension of date for forming internal complaint committee as per provisions of the POSH Act, 2013 .As per the State Government's order, all the employers of workplaces in the District of Mumbai City employing 10 or more needed to form internal compliant committee and register with the department on or before 20 July 2019. Non-compliance of the same could attract penalty of ₹ 50,000/- apart from cancellation of business licenses.

EVENTS

From 5th July to 3rd August 2019, Chamber organised many events which have met with overwhelming response. We had organised a live screening of presentation of the Budget 2019 by the Finance Minister at the Chamber's office on 5th July followed by a Public Meeting on the Union Budget jointly with six other organisations and a half day workshop on Direct Tax related provisions of Finance Bill (No. 2), 2019 jointly with the WIRC of ICAI and eminent professionals were the speakers for this workshop.

There were as many as three webinars, on Revised Foreign Liabilities and Assets information reporting (FLAIR) System, Practical issues regarding GST annual return and GST audit and on the Niceties of Presumptive taxation. All the three webinars had very good participation. Three study Circle/Study Group meetings by various committees also had very good enrolment and discussion.

Full day seminar on section 195 was organised by the International Taxation Committee had excellent response and participants were immensely benefited by the vast knowledge of the eminent speakers who were invited

For the past few years, the Chamber has been organising programs at the door steps of the outstation members and one such program on GST Annual Return and GST Audit was organised at Kolhapur.

Considering the ongoing audit season, we have organised seminar on tax audit on 17th August and audit under the Companies Act on 7th September at Mumbai and Nashik, Full day seminar on Charitable Trusts jointly with Bombay Chartered Accountants Society on 14th September. Members are requested to take benefit of these seminars.

We need the Almighty to bless all good beginnings at the Chamber. A Satyanarayana puja was performed on 20th July 2019 at the office of the Chamber. the office bearers and their families, the staff, Past Presidents and members participated in puja. We also had the President of BCAS CA Manish Sampat and Treasurer CA Abhay Mehta coming and wishing us.

This issue of the Journal is on the Insolvency and Bankruptcy Code. We had brought out a Special Issue on this topic when the law was enacted but it is still evolving and there have been many changes in the statute including the recent amendments and therefore, this issue, dealing with the updates thereto, will, I am sure, be useful for the readers.. I compliment and thank everyone involved in designing this issue and thank all the eminent authors for their valuable contribution.

Wishing you and your family A Happy Independence Day and A Happy Raksha Bandhan! By the time you read this, the Independence Day and Raksha Bandhan would have been celebrated. But with the long weekend, I am sure the celebrations would be on!

I would like to end this communication with a Management Quote

"Divide and rule, a sound motto,

Unite and lead, a better one"

Jai Hind!

VIPUL K. CHOKSI
President

Overview of IBC

CA Abizer Diwanji

The Insolvency and Bankruptcy Code, 2016 is probably one of the most important legislative reform of our time and paves the way for effective resolution of debt defaults across a spectrum of creditors. This is the first remedial action which spreads across various laws which was used by promoters to delay an eventual liquidation or a reconstruction. Whilst BIFR or liquidation took years to resolve, average resolution period under IBC has come down to 330 days, the very basis of the amended IBC regulation approved by Parliament yesterday.

As rightly stated in the IMF-World Bank Financial Sector Assessment Programme, January 2018, *"The Code consolidated and amended the laws relating to reorganization and insolvency resolution of corporates, partnership firms and individuals in a time bound manner, and for maximization of value of the asset. The Code requires that bankruptcy process to be completed within 180 days (with an option to extend for further 90 days) or else the borrower's asset may be sold to repay creditors. The new regulator, Insolvency and Bankruptcy Board of India, exercises regulatory oversight over insolvency professionals, insolvency professional agencies and information utilities".*

The Code introduces a shift from the earlier 'Debtor in possession' regime to a 'Creditor in control' regime represented by the Committee of Creditors (CoC). While highlighting this paradigm shift in law, the Hon'ble Supreme court in case of *Innoventive vs. ICICI Bank* observed: *"Entrenched managements are no longer allowed to continue in management if they cannot pay their debt".* This concept has enabled better flow of information between various stakeholders and led to effective resolutions. Before the code, the RBI had introduced a number of effective measures most of which failed due to lack of faith in the system by various stakeholders. A court driven, independent professional and a committee of creditors has ensured effective implementation of the law and led to better resolutions.

However, a balanced view would also demand discussion around the frustrations that have happened. Delayed court timelines mainly due to frivolous litigation have frustrated the process which at its core has time of essence. I would partly attribute this to the maturity of the various stakeholders and an immediate need to capacity build, not just in numbers but in competence be it regulators, courts, professionals, creditors and Corporate debtors themselves. There was a discussion around the fact that IBC was introduced when the stakeholders were not mature leading to heightened litigation and hence frustration of the very cause. I would argue that what we have done is exemplary, we built scale to deal with the magnitude knowing well that the maturity is lacking but over time have had the political will to implement the law in spirit. We are yet not there but will be in time as every frivolous effort has ultimately been dealt with firmly. We are dealing with a cultural shift where creditors need to accept that businesses can fail without fraud and where debtors need to accept that businesses will change hands on failure.

Progress so far

As of Mar 2019, 1,858 cases have been admitted under IBC out of which a staggering number of 1,143 are still ongoing while 94 cases have been closed through resolution

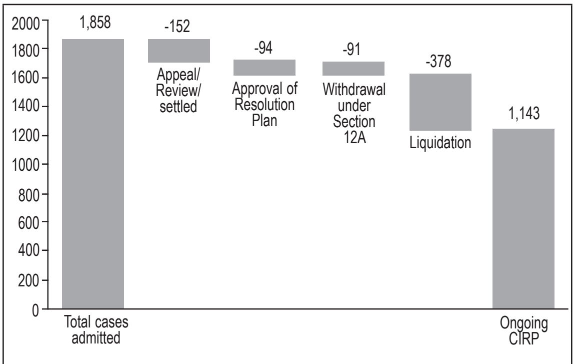

Chart 1 — Total cases under CIRP

Of the 1,143 ongoing CIRPs as on 31st March, 2019, 362 cases have been going on for more than 270 days, 186 cases are in the range of 181-270 days, 247 cases are in 91-180 day range while 348 cases are less than 90 days into CIRP. As the ecosystem matures and jurisprudence establishes, the timelines in completing the process should improve.

In 89 cases resolved, INR 1,46,674 crore of FC claims have been resolved at a recovery of 47% against liquidation value of 22%.

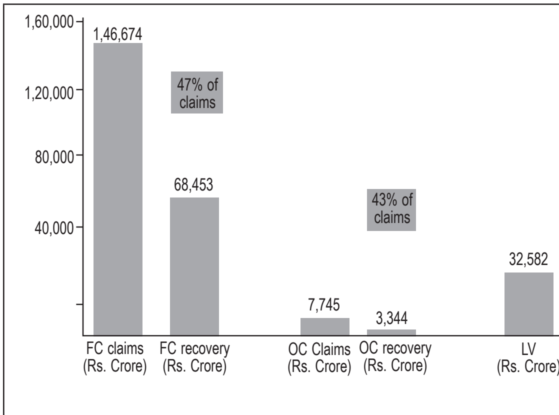

Chart 2 — Recovery for creditors

As on March 31, 2019, 920 (50%) cases were filed by Operational Creditors (OCs), 738 (40%) were filed by Financial Creditors and 200 (10%) were filed by Corporate Debtor. In January to March 2019 quarter, 172 cases have been filed by FCs in comparison to average 90 cases in the initial 3 quarters. The growing number of cases by the Financial Creditors indicate that the IBC has already struck a cord with the banks and financial institutions, who view the IBC as preferred mode to resolve distressed assets and maximise returns.

In terms of time taken for completion of resolution process, it has been seen that average timeline, in cases where resolution has been successfully completed, is 320 days

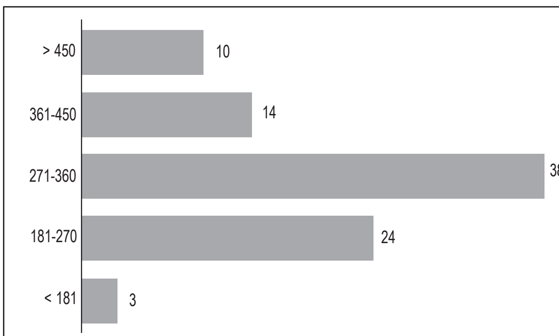

Chart 3 — Average days in successful resolutions

Cases have been filed across various sectors. 42% of cases filed are from the manufacturing sector covering industries like steel, Fast Moving Consumer Goods (FMCG), chemical products, electrical machinery, basic metals etc.; 30% in real estate and Engineering, Procurement and Construction (EPC) sector and 10% in trading companies. Other sectors under stress are textiles, power & utilities, FMCG, and hospitality. These are mostly late stage cases where overall sector has already been under stress due to several issues.

Key judgments that shaped the law

Personal Guarantees given for exposures to Corporate Debtors

The law of subrogation, a long standing principle that allowed personal guarantors to stake claim on the company for guarantee recoveries that banks could claim from the Corporate Debtor. This was mainly under the premise that the guarantee was given for the business as once control ceases, there would always be a claim on businesses. This resulted in resolution applicants resisting this liability contractually and banks actually not proceeding against **personal guarantees.**

***"It was not the intention of the legislature to benefit the 'Personal Guarantors' by excluding exercise of legal remedies available in law by the creditors, to recover legitimate dues by enforcing the personal guarantees, which are independent contracts"* - NCLAT**

Personal Guarantees now can be enforced against the Corporate Debtor by the Banks without any ultimate fall back on a resolution applicant. In my opinion, this is a welcome judgment wherein the very nature of personal guarantees is respected. However, given that personal guarantees, which until now were given as a formality, will no longer be forthcoming as the risk of invocation is real.

Rights of Home buyers

Homebuyers argued that they were in a unique position where Financial creditors would have a priority in recovery on assets which were partially sold to them and for which part payment was made by them. This resulted in significant public agitation in the CIRP of a land developer. The courts turned sympathetic to the Homebuyers recognising their plight. The IBC got amended to give home buyers a status of financial creditors and included them in the committee of creditors on a representation basis with voting rights. However, subsequently one did not see any decisiveness in the home buyers and plans kept getting delayed. A second amendment to IBC dragged dissenting voters towards a majority vote and also included a condition around voting based on "present and voting basis" hence avoiding abstention which was a big cause of indecision.

The whole concept of preferential treatment to home buyers is faulty. The fact that there is a resolution, home buyers would be the first to get their homes, which incidentally should be their prime objective, not recoveries. Secondly, involving retail home buyers in creditor decision making is never a good idea and even the Supreme court in Swiss Ribbons has established the fact that financial creditors are more savvy than operational creditors, which essentially what home buyers are, at least all across the world.

Personal guarantee being used by promoters to protect their assets

In many cases, since guarantees for loans of corporates are given by its promoters/directors in the form of personal guarantees, if there is a stay on actions against their personal assets during a Corporate Insolvency Resolution Process, such promoters/directors (who are also corporate applicants) may file frivolous applications to merely take advantage of the stay and guard their assets.

The Courts ruled that as per section 128 of the Indian Contract Act, the liability of the surety is co-extensive with that of the principal debtor and the creditor may go against either the principal debtor, or the surety, or both, in no sequence. It also observed that such contracts have a remedy against both the surety and the corporate debtor, without the obligation to exhaust the remedy against one of the parties before proceeding against the other, is of utmost importance for the creditor and is the hallmark of a guarantee contract, and the availability of such remedy is in most cases the basis on which the loan may have been extended.

The object of the Code is not to allow such guarantors to escape from an independent and co-extensive liability to pay off the entire outstanding debt, which is why Section 14 is not applied to them." – Hon. Supreme Court

This ruling has enabled many creditors to proceed against personal guarantees of a corporate debtor even during CIRP period as the moratorium is only for the Corporate Debtor. However, should a claim be admitted that guarantee can then be enforced only for the remaining amount.

Withdrawal of application u/s. 12

Section 12A provides for withdrawal of the application admitted with the approval of 90% voting share of CoC. Regulation. 30A(1) requires that the application for withdrawal shall be submitted before issue of Invitation for EOI. CoC shall consider the application within 7 days of its constitution or 7 days of receipt of application, whichever is later.

This section was contested in the courts on many counts. Firstly there was a view that it violated article 14 of the Constitution of India which gives and equal rights and hence section 12A in a regular settlement. This was negated by the Supreme court of India.

Further, there was enough debate that Regulation 30A(I) cannot stipulate conditions in addition that those prescribed by the main act. This was supported by the courts and hence the regulation was later removed.

The intent if section 12A was basically to give the financial creditors a right to pull the company out of CIRP if in their judgment, it would help better recoveries. However, the section imposes immense responsibility on the creditors and the courts to selectively approve such withdrawal only on an exceptional basis. The Essar case was a case in point where creditors and courts did not entertain a 12A offer of the promoters as they did not believe the facts supported the spirit of section. Another important aspect is that the prerogative of a 12A withdrawal is that of the creditor applicant and not the promoters of the corporate debtor.

Section 29A related issues

Section 29A of the IBC effectively debars existing promoters or their connected persons from bidding for a company under CIRP. This has been a much debated and much discussed section and is unprecedented anywhere else in the work. The maxim, businesses can fail, has been violated by this section by making it applicable to all defaulters as against only wilful ones. Whilst it is understandable that every promoter is not a wilful defaulter and there have been many business-related changes which may have resulted in defaults, the section seems to be bar most promoters for bidding for their companies in CIRP. This has caused much upheaval especially in the first 12 and the other 28 cases as promoters have not been used to giving up their businesses. This also led to many litigations and even an amendment to Section 29A to allow certain categories of bidders and relaxing the related party definition. Still 29A is the biggest bone of contention and fought aggressively in the courts

Issues revolved around:

- Constitutional validity
- Retrospective in nature
- Prevents maximisation of value of assets by not allowing erstwhile promoters to bid
- NPA criteria is arbitrary in nature

- Relatives having no business connection with erstwhile promoters are rendered ineligible

"Section 29A is constitutionally valid" – Supreme Court as

- A resolution applicant has no vested right for consideration or approval of its resolution plan and, therefore, no vested right is taken away by Section 29A.
- A person, who is unable to service its own debt beyond the grace period, is unfit to **be** eligible to become a resolution applicant. *"If the blind lead the blind, both shall fall into the ditch."*
- Neither can the period of one year be found fault with, as this is a policy matter decided by the RBI and which emerges from its Master Circular, as during this period, an NPA is classified as a substandard asset.
- The categories of persons who are collectively mentioned as 'relative' in *explanation* to section 5 (24A) need to have a connection with the business activity of the resolution applicant. In the absence of showing that such person is "connected" with the business of the activity of the resolution applicant, such person cannot possibly be disqualified under Section 29A(j).

Differences between Financial and Operating creditors

Sec. 5(7) of the Code defines financial creditors (FCs) as any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to. Sec. 5(20) of the Code defines Operational Creditors (OCs) as a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred

The Petitioners contested that there is no real difference between. FCs and OCs -- Both type of creditors give either money in terms of loans or money's worth in terms of goods and services to help run the CD as a going concern.

Judgment: "Classification is neither discriminatory, nor arbitrary, nor violative of Article 14" as

- Nature of loan agreements with FCs is different from contracts with OCs for supplying goods or services.
- FCs generally lend finance on a term loan or for working capital that enables the CD to either set up and/or operate its business. On the other hand, contracts with OCs are relatable to supply of goods and services in the operation of business. FCs can engage in restructuring of the loan as well as re-organisation of the CD's
- There is difference in dispute resolution of FCs and OCs. Contracts with OCs can and do have private arbitration clauses for dispute resolution, whereas, in loan contracts no such facility.
- Goods supplied or services provided by OCs may be substandard or goods may not have been supplied at all. These *qua* operational debts are matters to be proved in arbitration or in the courts of law. On the other hand, financial debts made to banks and financial institutions are well-documented and defaults made are easily verifiable.

No change in the power or role of the OC in a CIRP

Sec. 21 of the Code provides for the constitution of the CoC which shall comprise all financial creditors (FCs) of the CD. Sec. 30(4) of the Code requires CoCs to approve a resolution plan by a vote not less than 66% of voting share of the FCs. The approved resolution plan by CoC and Adjudicating Authority is binding on all stakeholders (including OCs).

The Petitioner contented that there is discrimination against OCs as they do not have a single vote in the CIRP. OC's are an important stakeholder in the resolution of CD

Judgment: "OCs are not discriminated against or Article 14 has not been infracted" – Supreme Court as:

- The FCs are in the business of money lending, they are best equipped to assess viability and feasibility of the business of the CD;
- OCs, who provide goods and services, are involved only in recovering amounts that are paid for such goods and services;
- The CoC has the primary responsibility of financial restructuring. It assesses the viability of a CD by taking into account all available information as well as to evaluate all alternative investment opportunities that are available. It evaluates the resolution plan on the basis of feasibility and viability.
- The NCLAT has, while looking into resolution plans approved by the CoC, always gone into whether OCs are given roughly the same treatment as FCs, and if they are not, such plans are either rejected or modified so that the OC's' rights are safeguarded.
- Reg. 38 strengthens the rights of OCs by statutorily incorporating the principle of fair and equitable dealing of their rights, together with priority in payment over FCs.

Commercial wisdom of the CoC given paramount importance without any judicial intervention

There have been numerous cases including Swiss Ribbons where the Courts have ruled that Commercial judgment should reside with the CoC. Also the Courts have ruled that litigation around cases should not be entertained by the courts until after a Resolution Plan, approved by the CoC. The latest amendment of the IBC regarding filing of resolution plans approved by CoC within 330 also seems to reiterate that.

Court judgments have supported that on the following grounds:

- Upon receipt of a rejected resolution Plan by the CoC, AA is obligated to initiate Liquidation under 33(1)
- Courts have not been conferred with the jurisdiction or authority to analyse or evaluate commercial decisions of the COC muchless to inquire into the justness of rejection of the resolution plan by the dissenting FCs
- The Courts have been endowed with the jurisdiction to reverse the commercial wisdom of the dissenting FCs
- Discretion of the Courts is limited to scrutiny of an approved resolution plan. even in that enquiry, the ground on which Courts can reject the resolution plan is under Sec. 30(2)
- Functions of IBBI do not directly or indirectly, pertain to regulating the manner in which the FC ought to or ought not to exercise their commercial wisdom during voting on the resolution plan

The recent amendment bill that is now law.

The Union Cabinet approved a proposal to introduce a Bill in the Parliament to carry out 8 amendments to the Insolvency and Bankruptcy Code, 2016. The amendments aim to fill critical gaps in the corporate insolvency resolution framework. The Government intends to ensure maximization of value of a corporate debtor as a going concern while simultaneously adhering to strict timelines.

The proposed amendments are:

- Clarity on allowing comprehensive corporate restructuring schemes such as mergers, demergers, amalgamations etc as part of the resolution plan. This may open up the route where corporates can propose business mergers (of subsidiaries, demergers of unrelated businesses for sale or amalgamations as they deem fit to make the business value accretive). However, creditors would be vary of bankruptcy remote structures where their assets may be alienated.
- Greater emphasis on the need for time bound disposal at application stage. This is just an assertion and aimed at court interpretations that the 14 day admit period is only directionary and not mandatory whilst the law does make it mandatory
- A deadline for completion of CIRP within an overall limit of 330 days, including litigation and other judicial processes. This amendment may have practical challenges as the right to appeal cannot be taken away. An emerging interpretation is that 330 days would be the timeline for filing an approved resolution plan with the courts and thereafter the plan can be contested. However, courts would need to understand the spirit of timely resolution and its consequent impact on the economics and not entertain much litigation.
- Votes of all financial creditors covered under section 21(6A) shall be cast in accordance with the decision approved by the highest voting share (more than 50%) of financial creditors on present and voting basis. This has been discussed above in the home buyers case.
- A specific provision that financial creditors who have not voted in favour of the resolution plan and operational creditors shall receive at least the amount that would have been received by them if the amount to be distributed under the Resolution Plan had been distributed in accordance with section 53 of the Code or the amount that would have been received if the liquidation value of the corporate debtor had been distributed in accordance with section 53 of the Code, whichever is higher. This will have retrospective effect where the resolution plan has not attained finality or has been appealed against.
- Inclusion of commercial consideration in the manner of distribution proposed in resolution plan, within the powers of the Committee of Creditors.
- Clarity that the plan shall be binding on the all stakeholders including the Central Government, any State Government or local authority to whom a debt in respect of the payment of the dues may be owed.
- Clarity that the Committee of Creditors may take the decision to liquidate the corporate debtor, any time after constitution of the Committee of Creditors and before preparation of Information Memorandum.

In conclusion

The law has come a long way in firstly having an effective insolvency regime and also an effective one. What mature economies achieved in 10-20 years, India is likely to achieve in less than 5 years. Our stakeholders are maturing by the day and as long as the courts, Insolvency professionals and the creditors are able to stick to the spirit of the law which centres around quicker resolution of stressed assets, we will see better realisations for financial creditors, continued support of operating creditors and sustenance of employment and capacities for the Indian Economy.

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Basis of Admission/Rejection of Application under IBC

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Present economic & legal scenario

Key to successful economic transformation lies in having a holistic picture about the challenges facing the economy and then synchronising specific policy responses with the right opportunities for making these interventions.

In recent past, our country has grown with macroeconomic stability. The country has also registered high growth rates with low inflation. Recent Union Budget has targeted a 5 trillion dollar economy by 2024-25.

Besides that the business environment to be conducive, laws of the country contribute to a large extent in getting more investments, expansions and sustainability.

The present Government has made a lot of effort and attempts to bring new laws, discard unwanted laws, repeal or amend old laws.

As one of an attempt to release huge sums of money that was stuck for years innumerably, the Insolvency and Bankruptcy Code, 2016 (**'IBC'**/**'Code'**) was enacted.

Introduction & Background

Prior to the enactment of IBC, the Personal and Corporate Insolvency/Bankruptcy in our country was scattered among different enactments like Presidency Towns Insolvency Act, 1909, the Provincial Insolvency Act, 1923, the Sick Industrial Companies (Special Provisions) Act, 1985 (**'SICA'**), etc. Presidency Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1923 still persists and the individuals are still governed by these Acts, till IBC is made applicable to individuals and partnerships.

There are other enactments such as the Recovery of Debts and Bankruptcy Act, 1993 and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (**'SARFAESI'**), which subsists along with IBC.

Prior to enactment of IBC, the Corporate Insolvency was mainly governed by various provisions such as the Companies Act, 1956 & then Companies Act, 2013, the LLP Act, 2008, SICA, etc.

There has always been a tug-of-war between a creditor and a debtor. The creditor would prefer to recover its money in the shortest possible time and the debtor, for more than one reason, would prefer deferment of payment to the creditor.

Various forums and multiple laws

As a tool of recovery, the creditors resort to either by filing summary suit under Civil Procedure Code before Civil Court or file winding up petition under the Companies Act before the High Court or file insolvency petition or even resort to filing police complaint to make recovery faster. In big cases with huge amounts involved, the Enforcement Directorate, Crime Branch, Directorate of Revenue, SFIO, etc., investigates to unearth the fraud. Accordingly, the matter remains pending either with Civil Court or High Court or Arbitrator or Magistrate/Sessions Court or MPID (Maharashtra Protection of Interest of Depositors in Financial Establishments Act, 1999) Special Court or Adjudicating Authority under PMLA (Prevention of Money Laundering Act). The Debtor, on the other side, *inter-alia*, used to file an application before the Board of Industrial and Financial Reconstruction ('BIFR'), where the matter would be kept lingering for years together in the name of reorganisation and reconstruction, besides resorting to other unscrupulous means.

This, to a certain extent has been curtailed by IBC through the *non-obstante* clause in Section 238 of IBC.

All in all, with so many enactments and agencies in place, the creditor has various avenues open for it to recover its money through different forums, which would help recovery in the shortest possible time and hence allows it to do forum shopping. Equally, the debtor had/has also means to defer the payment through few of such forums.

Such forums may be limited to those existing within nation or may be transnational forums.

Recently, petition against ***Jet Airways*** was admitted in Noord Holland district court, Netherlands, before it got admitted in NCLT, Mumbai. Notably, the NCLT, Mumbai, rejected an intervention application filed by a trustee appointed by a Netherlands Court, who pointed out that Noord Holland District Court had passed an order of bankruptcy against Jet on 21st May, 2019. The intervener submitted that it has appointed the Indian law firm to assist in taking control of the Corporate Debtor and its assets in India under the bankruptcy law of Netherlands and therefore sought for dropping the resolution process here in India, to avoid multiplicity of proceedings.

Rejecting the intervention, the NCLT, Mumbai said that Sections 234-235 of IBC, 2016, which deal with cross border insolvency process, was yet to be notified and further stated that in the absence of reciprocal arrangements under the yet to be notified, the foreign court could not have company bankrupt, and hence the order of Netherlands court was a nullity. An appeal to NCLAT has been filed by the Dutch insolvency administrator that insolvency proceedings against Jet Airways be recognised in the Company's insolvency proceedings in India.

In another case, 2 Writ Petitions were filed before the Madras High Court in the matter of ***M/s. Anandram Developers Private Limited (1st Petitioner) and Mukundan Vijayan (2nd Petitioner) vs. NCLT, Chennai (1st Respondent) and M/s. ARCIL (2nd Respondent)*** with the following prayers:

Prayer in W.P. Nos. 29084/2017 & 29085/2017: Writ Petitions filed under Article 226 of the Constitution of India, praying for a Writ of Mandamus, forbearing the 2nd Respondent and 1st Respondent from proceeding further with the Application filed by the 2nd Respondent in Application No. 603/2017 under Section 7 of IBC before the 1st Respondent to initiate corporate insolvency resolution process against the Company pending disposal of OA filed by the 2nd Respondent in OA 29/2016 on the file of DRT-I, Chennai, and Review Application No. 3 of 2017 in OA No. 430/2014 on the file of DRT-II, Chennai and consideration of the One Time Settlement Proposal given by the 1st Petitioner Company.

Besides other contentions of the Petitioners, further contention of the Petitioners was that the action of the 2nd Respondent in approaching the NCLT, would amount to forum shopping, also cannot be countenanced, for the reason, Insolvency and Bankruptcy Code, 2016, has been enacted, consolidating various enactments, such as Sick Industrial Companies (Special Provisions) Act, 1985; the (present) Recovery of Debts and Bankruptcy Act, 1993; the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002; Companies Act, 2013; Insolvency and Bankruptcy law and other laws.

The Hon'ble Court, *inter alia*, referred to various sections under IBC and regulations and rules framed thereunder including section 231 and section 238 of the IBC. Section 231 bars jurisdiction of other courts and section 238 is a *non-obstante* clause.

Contention of the Petitioner's counsel that applications are mechanically admitted was not accepted. Contention that approach of the 2nd Respondent to NCLT amounts to forum shopping is not tenable, as the Code enables filing of an application, notwithstanding the pendency of any proceedings, under the SARFAESI Act, 2002. When the Code has not been stayed, the process envisaged in the Code, has to be continued, and cannot be restrained.

The Court after hearing both the sides and the various decisions quoted by each party was not inclined to entertain the writ petitions and the same were dismissed.

There may be various forums available where a claim or case may be proceeded with, where remedy may lie; but the "objectives" in several of the enactments, under which the forums are formed, may vary. There may also be overriding effect/repugnancy/inconsistency among two or more central legislations or may be between the state legislations and central legislations.

Such inconsistencies in various laws and their respective adjudicating authorities therefore give rise to opportunity of forum shopping.

In the matter of ***Nitin Gupta vs. Applied Electro-Magnetic (P) Ltd.***, when an application was made by an employee under section 9 of IBC for non-payment of the salary by the Corporate Debtor, who in turn objected that before the Adjudicating Authority regarding forum shopping, the NCLT, Delhi Bench had held that there is no law that an unpaid employee who has made a complaint before the Labour department cannot move application under the Code for initiation of CIRP against the employer.

The recent judgment of NCLAT passed in the matter of ***Rotomac Global Private Limited, (through Anil Goel, Liquidator) as the Appellant vs. Deputy Director, Directorate of Enforcement as Respondent,*** is a good example wherein Bank of Baroda had initiated Corporate Insolvency Resolution Process ('CIRP') against *'Rotomac Global Private Limited'* ('Corporate Debtor'). The Adjudicating Authority ordered for liquidation of the Corporate Debtor and liquidator got appointed. The Directorate of Enforcement during the investigation found that accused persons having misappropriated/diverted bank funds, committed criminal breach of trust and laundered the money so diverted.

The Directorate of Enforcement passed a Provisional Attachment Order attaching the properties provisionally lying in name of Corporate Debtor and its Directors contending that the properties in question fall within the definition of *'Proceeds of Crime'* in terms of *Section 2(1)(u) of the Prevention of Money Laundering Act, 2002* (**'PMLA'**) and hence provisionally attached and that the property provisionally attached constitutes the value of such proceeds of crime.

The Liquidator, on the other hand filed an application for direction on Directorate of Enforcement for release of assets of the Corporate Debtor.

The Appellate Tribunal after hearing, *inter alia*, stated that it is clear that the PMLA relates to 'proceeds of crime' and the offence relates to 'money-laundering' resulting in confiscation of property derived from, or involved in, money-laundering and for matters connected therewith or incidental thereto. Thus, as the PMLA or provisions therein relates to 'proceeds of crime', it held that Section 14 of the 'I&B Code' is not applicable to such proceedings.

This apart, NCLAT further stated that the attachments were made by the Deputy Director of Directorate of Enforcement much prior to initiation of the CIRP, therefore, the 'Resolution Professional' cannot derive any advantage out of Section 14.

It finally stated that as PMLA relates to different fields of penal action of 'proceeds of crime', it invokes simultaneously with the IBC, having no overriding effect of one Act over the other including the IBC and by dismissing the same finding no merit in the appeal.

Similar question had arisen for consideration earlier before this Appellate Tribunal in ***Varrsana Ispat Limited vs. Deputy Director, Directorate of Enforcement*** –wherein this Appellate Tribunal observed and *inter alia*, held that as PMLA related to different fields of penal action of 'proceeds of crime', and shall have no overriding effect of one Act over the other, including the IBC. Accordingly it dismissed the appeal.

Very recently JSW intends to seek immunity from NCLT from litigations against ***Bhushan Power and Steel***, which is being investigated by CBI for diversion of crores of Rupees. JSW is the successful bidder for ***Bhushan Power and Steel,*** but if certain assets of it is declared as *'proceeds of crime'* then it is going to be a difficult affair, since one would never know at this stage as to how much assets would be treated as such and how much would fall in JSW's kitty.

Given that Entry 9 of List III of the Seventh Schedule to the Constitution of India provides that both the Parliament and State Legislatures have legislative competence over "bankruptcy and insolvency", a possibility of inconsistency between such legislations arises.

In ***M/s. Innoventive Industries Ltd. vs. ICICI Bank***, the Hon'ble Supreme Court, dealt with the repugnancy in Insolvency and Bankruptcy Code, 2016 and Maharashtra Act, regarding "moratorium". Referring to Article 254 of the Constitution of India and a catena of case laws, the Hon'ble Supreme Court, *inter alia*, stated that the inconsistency must be clear and direct and be of such a nature as to bring the two Acts or parts thereof into direct collision with each other, reaching a situation where it is impossible to obey the one without disobeying the other. This happens when two enactments produce different legal results when applied to the same facts.

The only exception to the above is when it is found that a State legislation is repugnant to Parliamentary legislation or an existing law if the case falls within Article 254(2), and Presidential assent is received for State legislation, in which case State legislation prevails over Parliamentary legislation or an existing law within that State.

It was therefore made clear, that the earlier State law is repugnant to the later Parliamentary enactment.

Where an issue of repugnancy between the Maharashtra Relief Undertakings (Special Provisions) Act, 1958, which is a State law, and the Code arose, the Supreme Court in its judgment also laid down certain key principles to evaluate repugnancy of a State law with a Union law.

Further the Court also referred section 238 of the Code and held that the later non-obstante clause of the Parliamentary enactment will prevail over the limited *non-obstante* clause contained in Section 4 of the Maharashtra Act.

After discussing about forum shopping and overriding effect/repugnancy/inconsistency of various legislations, which could not have been discussed separately, let's look at few provisions under IBC, analyse the same with the circumstances when an application gets admitted, needs rectification, gets rejected, those disputed, etc. and simultaneously proceed to understand the basis of admission and rejection of applications filed under IBC and various case laws with reference to those provisions.

As per section 4 of IBC, the Code gets triggered the moment default is of rupees one lakh or more.

Initiation of corporate insolvency resolution process by financial creditor

Under **section 7**, a financial creditor either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, may file an application with a record of default/evidence, for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred in respect of a *financial debt.*

Section 7(5) provides that where the Adjudicating Authority is satisfied that – (a) a default has occurred and the application is complete and there is no disciplinary proceedings pending against the proposed resolution professional, it may, by order, admit such application; or (b) default has not occurred or the application is incomplete or any disciplinary proceeding is pending against the proposed resolution professional, it may, by order, reject such application.

The corporate insolvency resolution process shall commence from the date of admission of the application under section 7(5).

In ***Nikhil Mehta & Sons (HUF) vs. AMR Infrastructure Ltd.,*** the NCLAT examined the inclusive definition of 'financial debt' as defined u/s. 5(8) of IBC as a debt along with interest which is disbursed against the consideration for the time value of money and it may include any of the events enumerated under the provision.

Initiation of corporate insolvency resolution process by operational creditor

Under **section 8**, operational creditor has to deliver a demand notice on occurrence of a default of a debt, or a copy of an invoice demanding payment of the amount involved in the default to the corporate debtor.

The corporate debtor shall, within a period of ten days of the receipt of the demand notice or copy of the invoice bring to the notice of the operational creditor -

(a) existence of a dispute, if any, or record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute;

(b) the payment of unpaid operational debt by sending an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the corporate debtor or by sending an attested copy of record that the operational creditor has encashed a cheque issued by the corporate debtor.

As far as the Financial Creditor is concerned, there is no need of issuing any notice on the part of Financial Creditor to the Corporate Debtor before filing an application, which the Operation Creditor has to issue prior to filing an application before the Adjudicating Authority.

Under **Section 9**, after the expiry of the period of ten days from the date of delivery of the notice or invoice demanding payment, if the operational creditor does not receive payment from the corporate debtor or notice of the dispute, the operational creditor may file an application along with copies of invoice and other documents before the Adjudicating Authority for initiating CIRP.

The Adjudicating Authority may by order, either admit or reject the application as per the provisions.

The Adjudicating Authority may admit it if the application is *inter alia*, complete in all respect, there is no payment made of such operational debt, no notice of dispute is sent to operational creditor or there is no record of dispute in the information utility and may reject the application if the application is incomplete, payment unpaid operational debt has been made, the creditor has not delivered the invoice or notice for payment to the corporate debtor, notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility, after giving the applicant to rectify the defect, if any.

Accordingly, the CIRP shall commence from the date of admission of the application.

From above provisions of IBC, what we understand is that for a financial creditor or an operational creditor to make an application under IBC and establish its claim, there has to be a debt and a default that has occurred due to non-payment of debt. Further, a default may be of a financial debt or an operational debt.

Disputes and Limitation

Various types of disputes have been raised by the Corporate Debtors and each of the Adjudicating Authorities, Appellate Authority, High Courts and the Supreme Court has dealt with the same based on facts and circumstances in each case.

The Adjudicating Authority is required to examine before admitting or rejecting an application under Section 9 whether the 'dispute' raised by corporate debtor qualify as a 'dispute' as defined under section 5(6) and whether notice of dispute given by the corporate debtor fulfilling the conditions stipulated in sub-section (2) of section 8 of the Code.

The question as to what do 'dispute' and 'existence of dispute' mean for the purpose of determination of an application under section 9 of the Code fell for consideration before the Appellate Tribunal in ***Kirusa Software (P) Ltd. vs. Mobilox Innovations (P.) Ltd.*** The matter went up to the Supreme Court, which is discussed subsequently, and after this decision, the definition of dispute underwent change and the same has now been modified and become an inclusive definition.

There are catena of judgments on the admissibility or otherwise and various disputes raised by the corporate debtor.

In the matter of ***Gurcharan Singh Soni & Kuldeep Kaur Soni vs. Unitech Ltd. (NCLAT)***, an application was filed by the Appellants on the ground that the Consumer Dispute Redressal Commission had passed on order directed a real estate respondent company to refund the amount invested along with interest and also compensation and the amount lost in litigation. The Tribunal agreed that there was a debt due to the appellants and a default on the part of the respondent. But the amount due was not operational debt under section 5(21) of IBC. Therefore they did not come within the meaning of operational creditor. The application under section 9 of IBC was therefore rejected.

In ***KLA Construction Technologies vs. CRG Realty (NCLAT)*****,** affirming the decision of NCLT, Delhi, the Appellate Tribunal held that money payable as advance under the contract was not an operation debt.

In the matter of ***Bombay Stock Exchange Ltd. vs. Asahi Infrastructure & Projects Limited,*** the exchange had filed an application u/s. 9 of IBC for non payment of listing fees and NCLT, Mumbai, had dismissed the application stating that NCLT is not the right forum to initiate recovery proceedings for non-payment of listing fees.

Besides other disputes, prior to enforcement of Section 238A, there were disputes on the applicability of the Limitation Act, 1963 to the applications filed under IBC.

Section 238A was inserted w.e.f. 6-6-2018 and it states that the provisions of the **Limitation Act, 1963** (36 of 1963) shall, as far as may be, apply to the proceedings or appeals before the Adjudicating Authority, the National Company Law Appellate Tribunal, the Debt Recovery Tribunal or the Debt Recovery Appellate Tribunal, as the case may be.

The Supreme Court in ***B. K. Educational Services Private Ltd. (Appellant) vs. Parag Gupta and Associates (Respondents)***, before which the question was raised by the appellants in these appeals is as to whether the Limitation Act, 1963 will apply to applications that are made under section 7 and/or section 9 of the Code on and from its commencement on 1-12-2016 till 6-6-2018.

The Supreme Court after hearing, *inter alia*, concluded by stating that the Limitation Act has in fact been applied from the inception of the Code, it is unnecessary to go into the arguments based on the doctrine of laches. The Supreme Court therefore remanded the appeals to the NCLAT to decide the appeals afresh in the light of this judgment.

There is always a scope of a dispute in one way or the other depending upon the facts of each case, whenever any creditor, may be financial or otherwise initiates insolvency process. The scope of dispute is comparatively much less in case when financial creditor initiates the process than the operating creditor initiating the same.

Different benches of the NCLT provided conflicting interpretations to the terms 'dispute' and 'existence of dispute'. Finally the Supreme Court in ***Mobilox Innovations Pvt. Ltd. vs. Kirusa Software Pvt. Ltd.*** held that the definition of dispute is an inclusive one and also held that it would not be necessary for the dispute to be pending before the filing of the application since *"a dispute may arise a few days before triggering of the insolvency process, in which case, though a dispute may exist, there is no time to approach either an arbitral tribunal or a court."* To determine if the dispute exists, the court held that *"all that the adjudicating authority is to see at this stage is whether there is a plausible contention which requires further investigation and that the "dispute" is not a patently feeble legal argument or an assertion of fact unsupported by evidence…The Court does not at this stage examine the merits of the dispute except to the extent indicated above. So long as a dispute truly exists in fact and is not spurious, hypothetical or illusory, the Adjudicating Authority has to reject the application."* By virtue of the Second Amendment to the Code, the decision in Mobilox was given statutory recognition.

The Supreme Court, in the matter of ***Transmission Corporation of Andhra Pradesh Limited (Appellant) vs. Equipment Conductors and Cables Limited (Respondent),*** where there was an application under section 9 by the Operation Creditor, held and stated that:

"51. It is clear, therefore, that once the operational creditor has filed an application, which is otherwise complete, the adjudicating authority must reject the application under Section 9(5)(2)(d) if notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility. It is clear that such notice must bring to the notice of the operational creditor the "existence" of a dispute or the fact that a suit or arbitration proceeding relating to a dispute is pending between the parties. Therefore, all that the adjudicating authority is to see at this stage is whether there is a plausible contention which requires further investigation and that the "dispute" is not a patently feeble legal argument or an assertion of fact unsupported by evidence. It is important to separate the grain from the chaff and to reject a spurious defence which is mere bluster. However, in doing so, the Court does not need to be satisfied that the defence is likely to succeed. The Court does not at this stage examine the merits of the dispute except to the extent indicated above. So long as a dispute truly exists in fact and is not spurious, hypothetical or illusory, the adjudicating authority has to reject the application."

The Supreme Court in ***Innoventive Industries vs. ICICI Bank***, had also *inter-alia* held that *"at the stage of Section 7(5), where the adjudicating authority is to be satisfied that a default has occurred, that the corporate debtor is entitled to point out that a default has not occurred in the sense that the "debt", which may also include a disputed claim, is not due. A debt may not be due if it is not payable in law or in fact."*

It should be noted that wherever there is a plausible dispute between the parties, the same can be agitated before a civil court and that the adjudicating authority under IBC is not the right forum.

Whether IBC can be used for recovering money or is it merely a resolution mechanism?

Frankly, every individual or entity would make all possible attempts to recover its money through whichever means possible.

Though IBC is a resolution mechanism, whether IBC gives leeway to creditors to take a shape of a recovery mechanism? May be yes, but this is how money, which would have been otherwise blocked, is opened for circulation to boost the economy.

Though IBC cannot be used for recovering money, it has helped recovering huge amounts since its enactment.

In ***K. Kishan vs. Vijay Nirman Company Pvt. Ltd.***, the Court held that operational creditors cannot use the Code either prematurely or for extraneous considerations or as a substitute for debt enforcement procedures. The alarming result of an operational debt contained in an arbitral award for a small amount of say, two lakhs of rupees, cannot possibly jeopardise an otherwise solvent company worth several crores of rupees. Such a company would be well within its rights to state that it is challenging the Arbitral Award passed against it, and the mere factum of challenge would be sufficient to state that it disputes the Award. Referring to ***Mobilox*** judgment, it stated that such a case would clearly come within para 38 of ***Mobilox Innovations (supra)***, being a case of a pre-existing ongoing dispute between the parties. The Court further stated that "the object of the Code, at least in so far as operational creditors are concerned, is to put the insolvency process against a corporate debtor only in clear cases where a real dispute between the parties as to the debt owed does not exist".

The filing of section 34 (of Arbitration & Conciliation Act) against an Arbitral Award shows that a pre-existing dispute which culminates at the first stage of the proceedings in an Award, continues even after the Award, at least till the final adjudicatory process under sections 34 & 37 (of Arbitration & Conciliation Act) has taken place.

Conclusion

IBC has proved to be the shortest possible route compared to any of the earlier enactments. Still more to come is the cross-border insolvency and group insolvency.

Whatever one may perceive – a recovery tool or resolution mechanism – since the enactment of the IBC, a total amount of around ₹ 4 lakh crore has been recovered. You decide which way you treat.........

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> I have given you advice enough; now put at least something in practice. Let the world see that your reading of the scriptures and listening to me has been a success.
>
> – *Swami Vivekananda*

Financial Creditors

CA Sanat Jariwala & Ami Jain *Advocate*

POSITIONING OF FINANCIAL CREDITORS UNDER INSOLVENCY REGIME IN INDIA

The Indian legislature, accentuated by the alarming increase in the incidence of sickness in industrial companies and mounting non-performing assets in the banking sector, had enacted the "Sick Industrial Companies (Special Provisions) Act, 1985, (SICA) in the mid-eighties to counter the ill-effects of sickness in companies, such as loss of production, loss of employment, loss of revenue to the Central and State Governments and locking up of investible funds of banks and financial institutions. The said Act followed a three-pronged approach, i.e. to fully utilise the productive industrial assets; afford maximum protection of employment; and optimise the use of funds of banks and financial institutions to resuscitate and rejuvenate potentially viable sick industrial companies expeditiously. And, as a last resort, to salvage the productive assets and realise the amounts due to the banks and financial institutions from the non-viable sick industrial companies through winding up process of such companies.

The Board for Industrial & Financial Reconstruction (BIFR), however, failed to achieve the desired goals, especially in terms of desired recovery of defaulted loans by financial creditors comprising banks, asset reconstruction companies, NBFCs and, hence, an impelling need was felt to introduce a new enactment in place of SICA, which resulted in the birth of the Insolvency and Bankruptcy Code (Code), 2016, w.e.f. 1st December, 2016, with the concurrent repeal of SICA.

The oblique object of the Code is to consolidate and amend the laws relating to reorganization and insolvency resolution of limited liability entities forthwith in a time-bound manner for maximisation of value of assets of such entities; promote entrepreneurship; availability of credit; balance the interests of all stakeholders including alteration in the priority of payment of government dues and to establish an Insolvency and Bankruptcy Fund, and matters connected therewith or incidental thereto. An effective legal framework for timely resolution of insolvency and bankruptcy is expected to support development of credit markets and encourage entrepreneurship while improving 'Ease of Doing Business' and facilitating more investments leading to higher economic growth and development.

One of the most important and glittering features of the Code is that it places financial creditors on a much higher pedestal than any other stakeholder in the enterprise, not only in the matter of recovery of outstanding dues but also in terms of power to take all decisions which bind all other stakeholders as well.

DISENTITLEMENT FOR ACCEPTANCE AS FINANCIAL CREDITOR

A *sine qua non* of the Code is to prove that the creditor falls within the ambit and scope of the definition of 'Financial Creditor' u/s. 5(7) and 'financial debt' u/s. 5(8) of the Code to be regarded as a 'financial creditor'.

Any creditor who has a financial debt as defined u/s. 5(8) of the Code recoverable from a corporate debtor, which is in default within the meaning of Section 3(12), is a 'financial creditor' eligible to file an application under Section 7 of the Code. The ingredients to be satisfied are:

a. That there has to be a recoverable debt as defined u/s. 3(11) of the Code;

b. Such debt must be a financial debt as defined in Section 5(8) of the Code which, *inter alia*, demands that debt along with interest, if any, is disbursed against consideration of time value of money; and

c. That there is a default within the meaning of section 3(12) of the Code.

According to Section 5(8) of the Code, it is incumbent upon the creditor to demonstrate from the material on record or otherwise that it is a financial transaction in which the defaulted debt had been disbursed to the corporate debtor against consideration for time value of money and it is therefore entitled to invoke the corporate insolvency resolution process (CIRP) in terms of Section 7 of the Code. To illustrate:

- The National Company Law Tribunal (NCLT), New Delhi, rejected an application filed u/s. 7 of the Code by Nikhil Mehta & Sons (HUF) & others against AMR Infrastructure Ltd., holding that there was no time value of money notwithstanding "Assured Returns" by the developer as the ingredients including applicability of interest were mercifully missing. NCLAT, after analysing the gamut of the provisions of the Code, set aside previous verdicts of NCLT, New Delhi, and considered realty buyers as financial creditors (FCs) who are entitled to be recognised as such, as the developer had promised 'committed/assured returns' as a part of the deal which had the commercial effect of borrowing [Section 5(8)(f)](Appeal No. 7/2017). It is well-accepted that if the debt is not on account of disbursement nor carries either interest or has any provision having commercial effect of such lending, such debt will be clearly outside the realm and definition of 'Financial Creditor' u/s. 5(7) and 'financial debt' u/s. 5(8) of the Code.

- The National Company Law Appellate Tribunal (NCLAT) by its order passed 4th July, 2018, in Appeal No. 311/2018 in the matter of Shreyans Realtors held that although the applicant (financial creditor) had resolved to grant loan to the corporate debtor on interest, but as the corporate debtor had not accepted payment of any interest on the amount borrowed by it, the applicant lender cannot claim to be the financial creditor and, hence, declined to interfere with order passed by NCLT rejecting the application of the applicant filed in capacity of the FC.

- A creditor who disbursed loan for time value of money, say on interest, to any entity against the corporate guarantee furnished by the corporate debtor is also an FC. This contention receives strength and support from the verdict delivered by NCLAT in Appeal No. 61/2018 in the matter of *Andhra Bank vs. F. M. Hammerle Textile,* where NCLT had rejected the plea of the bank holding corporate guarantee of the corporate debtor for securing loans provided to *Vardhman Polytex Ltd., inter alia*, on the ground that the claim of the bank may arise when the guarantee is invoked and that there was no default committed by the borrowing company. However, in appeal before NCLAT, the said order of NCLT was set aside, holding that Andhra Bank is an FC as there is counter-indemnity obligation in respect of guarantee given by the corporate debtor.

- In a historic judgment, NCLAT set aside the order passed by NCLT, admitting the application u/s. 7 of the Code filed by a creditor, in Appeal No. 142/2017 in the matter of *Neeraj Bhatia vs. Davinder Ahluwalia & others,* holding that 'personal guarantor' as defined in Section 5(22) cannot claim to be a 'Financial Creditor' as defined u/s. 5(7) read with Section 5(8) of the Code as the amount is paid to the Bank (Financial Creditor) as a 'personal guarantor' which was not disbursed against the consideration for time value of money. Section 140 of Indian Contract Act confers the right of subrogation on guarantor / surety who, on making payment to the creditor on behalf of the principal debtor, steps into the shoes of the said creditor (who may be a financial creditor) and who has the same right and remedy as the said creditor had against the principal debtor. It remains to be seen as to whether this vital aspect can have any bearing on said decision rendered by NCLAT. It may be noted that the term 'Financial Creditor' includes even a person to whom the debt is assigned or transferred.

- NCLT, Mumbai, had an occasion to determine whether or not Phoenix ARC, (which was the assignee of loans granted by its predecessor to the holding company of Doshion Water Solution Pvt. Ltd., corporate debtor), was an FC as a result of the collateral security it had in the form of pledge of shares provided by the corporate debtor to it for securing loans given to its holding company. NCLT ruled that Phoenix ARC was not an FC as the debt facility was given to the holding company and not to the corporate debtor and that the liability of the corporate debtor was restricted to the pledge of shares [CP No. 1752/2017 in the matter of Doshion Water Solutions P. Ltd.]. Earlier, NCLT, Allahabad, in CA No/81/2018 in CP No. (IB) 77/ALD 2017 had, in the matter of *ICICI Bank vs. Anuj Jain,* (Resolution Professional for Jaypee Infratech Ltd.), rendered a similar decision where a similar issue was decided by them. The decision of Mumbai Bench was carried to NCLAT in appeal by Phoenix ARC where NCLAT upheld the judgment passed by NCLT, holding that pledge of shares does not amount to disbursement of any amount against consideration for time value of money and does not fall within Section 5(8)(f) of the Code (Appeal No. 325/2019). Phoenix ARC has now assailed the orders passed by NCLT and NCLAT before the Hon'ble Supreme Court, which is presently pending.

- In another judgment, NCLT, Mumbai, dismissed the petition filed by the Oriental Bank of Commerce in CP No. 469/2018 in the matter of Ruchi Global Ltd. on the ground that the same was not maintainable. The legal principle adumbrated in the said decision appears to have been on the basis that when parties enter into a valid and lawful contract, they are under an obligation to abide by the same and merely because a move is made under the Code, it does not discharge the parties from a lawful obligation. The Bench further noted that u/s. 7 of IBC, "a financial creditor either by itself or jointly with other financial creditors may file an application….". A joint application under IBC ought to be filed with the consent of all other interested parties whereas in the said case, the financial creditor appeared to have filed the petition u/s. 7 on its own, without having consulted or without having approval of rest of the members of the consortium.

- In another landmark judgment in Appeal No. 346/2018 in the matter of Vishnu Kumar Agarwal, NCLAT, while observing that there is no bar in the Code for filing two applications simultaneously u/s. 7 against the 'Principal Borrower' as well as the 'Corporate Guarantor(s)' or against both the 'Guarantors', held that once an application u/s. 7 filed by the 'Financial Creditor' is admitted against one of the 'Corporate Debtor' ('Principal Borrower' or 'Corporate Guaran-tor(s)'), second application by the same 'Financial Creditor' for same set of claim and default cannot be admitted against the other 'Corporate Debtor' (the 'Corporate Guarantor(s)' or the 'Principal Borrower'). Further, though there is a provision to file joint application u/s. 7 by the 'Financial Creditors', no application can be filed by the 'Financial Creditor' against two or more 'Corporate Debtors' on the ground of joint liability ('Principal Borrower' and one 'Corporate Guarantor', or 'Principal Borrower' or two 'Corporate Guarantors' or one 'Corporate Guarantor' and other 'Corporate Guarantor'), till it is shown that the 'Corporate Debtors' combined are a joint venture company. In view of the said decision which is currently pending by way of challenge before Supreme Court, FCs have to make a judicious assessment to determine as to which out of two proceeding under insolvency law, one against the corporate debtor and second against guarantors, would ensure higher and quicker recovery by them.

ARE FINANCIAL CREDITORS ABLE TO CALL SHOTS AND STEER THE COURSE OF CIRP?

At the heart of the Code is the Committee of Creditors (CoC) comprising financial creditors (operational creditors in the absence of financial creditors or, as prescribed under the Code), who have been empowered to decide the fate of financially-distressed corporate debtors, albeit with a rider of securing minimum 66% of the total voting share of such FCs in favour of any decision. The decision to revive a corporate debtor under IBC or to sound its death-knell lies with the CoC, with complete leverage now being accorded to them by the apex court insofar as their 'commercial wisdom' is concerned. This is a recent development as prior to the judgment of the Hon'ble Supreme Court in the matter of *K Sashidhar vs. Indian Overseas Bank [2019] 152 SCL 312 (SC)*, an Adjudicating Authority (AA) could satisfy itself about the commercial wisdom of the CoC as well while approving/rejecting a resolution plan. The apex court's ruling in *K Sashidhar (supra)* has undoubtedly crowned the financial creditors as king or, king-makers, as their wisdom in the matter of decisions taken in regard to the future course of action with respect to a corporate debtor and sealing its fate are unquestionable and non-justiciable. The power bestowed, however, is not unbridled as the CoC's actions/decisions are required to be within the framework of the law while approving a resolution plan, i.e. the plan should not be in contravention of Sections 30(2) and 30(4) of the Code as also be in conformity with Regulations 37 through 39 of the IBBI (Insolvency Resolution for Corporate Persons) Regulations, 2016. As observed by the apex court in *K. Sashidhar (supra),* none of the specified functions of the Board, directly or indirectly, pertain to regulating the manner in which the FCs ought to or ought not to exercise their commercial wisdom during the voting on the resolution plan under Section 30(4). The riders, therefore, as expounded in brief by the apex court, could be with respect to the following: First, that the approved resolution plan is not in contravention of the provisions of any law for the time being in force. Second, there has been no material irregularity in exercise of powers 'by the resolution professional' during the corporate insolvency resolution period. Third, the debts owed to operational creditors have been provided for in the resolution plan in the prescribed manner. Fourth, the insolvency resolution plan costs have been provided for repayment in priority to all other debts. Fifth, the resolution plan complies with any other criteria specified by the Board. Further, the matters or grounds - be it u/s. 30(2) or u/s. 61(3) – are for testing the validity of the 'approved' resolution plan by the CoC; and not for approving the resolution plan which has been disapproved or deemed to have been rejected by the CoC in exercise of its business decision.

Although the apex court's decision in K. Sashidhar is a reflection of past judgments, which have refrained from questioning the 'commercial wisdom' of lenders/creditors, the authors feel that it is time to allow review of such decisions, to ascertain that the creditors/lenders have indeed applied their mind in the facts and circumstances of a given case. This, perhaps, has become essential today given the plight of the banking industry in the country which is reflected by unprecedented level of non-performing assets.

MORAL & LEGAL DUTIES OF FINANCIAL CREDITORS

A bare perusal of the Code leaves no room for doubt that FCs hold the rein for all stakeholders of the corporate debtor as there is a paradigm shift from the erstwhile management of a corporate debtor being in possession of stressed assets to creditors who now assume control from the erstwhile management through the resolution professional and are able to approve resolution plans of other better and more efficient managers, which would not only be in the interest of the corporate debtor itself but in the interest of all stakeholders, such as other creditors, workers, and shareholders other than shareholdings of the erstwhile management. There is an unwritten moral duty on the part of FCs to act judiciously while exercising the authority bestowed on them by the statute, especially in the process of selection of the successful resolution applicant and approval of the resolution plan which becomes binding on all concerned without their consent u/s. 31(1) of the Code. One of the underlying objects of the Code is to balance the interest of all stakeholders and given that all of them, barring financial creditors, have been left with no say, it is the paramount duty of FCs to be fair, equitable and transparent throughout the CIRP.

In its wisdom, NCLAT deemed it fit and proper to revise the distribution of the proceeds towards repayment of the restructured liabilities in the matter of ESSAR Steel Ltd. (Appeal No. 242/2019) and awarded 100% to operational and financial creditors whose claims were less than ₹ 1 crore as also workmen, whereas all other financial and operational creditors were granted around 60% of their admitted dues. The said order of NCLAT has been carried to Apex Court which will decide whether or not NCLAT's said order is sustainable in law. But in the meanwhile, Apex Court ordered on 22nd July, 2019 the stay of the impugned order and posted the case on 7th August, 2019 for further hearing.

Among legal duties, FCs are required to observe the rule of natural justice by giving a fair chance to the erstwhile management/promoters of the corporate debtor as also prospective resolution applicants concerned while approving or rejecting a resolution plan, given that their rights are going to be affected/prejudiced by the decision of CoC. Natural justice demands that decision should be passed on some evidence of probative value. The object underlying rules of natural justice is to prevent miscarriage of justice and secure fair play in action. It may be noted that NCLT, Chennai, disposed of an application filed by an unsuccessful resolution applicant in CP No. 689/2017 in the matter of Merchem Ltd. and directed CoC to consider its resolution plan afresh as the same was approved rejected in the absence of the said unsuccessful resolution applicant. It may be relevant to state here that qualifying resolution applicants have the right to be heard in CoC meetings as in terms of Section 30(5) of the Code, they are entitled to attend such CoC meetings. NCLT, Kolkata, in CP-(IB) No. 359/ KB/2017 on 04-5-2018 in the matter of *Binani Cement Ltd. vs. Mr. ijaykumar V. Iyer*, RP of Binani Cement. ruled that denying an opportunity to be heard to Ultra Tech (applicant) when CoC took a decision not to consider its plan for further negotiation is unfair and unjust and against the very objective of the Code. It continued saying that not scoring as H1 applicant (highest bidder) is not a disqualification for participating in the bidding process. NCLAT has, in Rajputana Properties Pvt. Ltd [I.A. No. 594 of 2018 in Company Appeal (AT) (Insolvency) No. 188 of 2018], held that CoC, while approving or rejecting one or other resolution plan, should follow such procedure which is transparent and that the resolution applicants are not mere spectators but may express their views to the CoC for coming to a conclusion in one or the other way.

It is the bounden duty of FCs to satisfy themselves about the viability and feasibility of resolution plans u/s. 30(4) before approving them. NCLT, Chennai, observed in their order in the matter of Merchem Ltd. (supra) that CoC did not appear to have recorded its reasons pertaining to the viability and feasibility of the resolution plan-submitted by the resolution applicant.

Regulation 39(3) of IBBI (Insolvency Resolution for Corporate Persons) Regulations, 2016, has been amended by Notification dated 3rd July, 2018, effective from 4th July, 2018, in terms of which it is now mandatory for CoC to record reasons for approving or rejecting a resolution plan. Said amended regulation further demands that CoC shall evaluate the resolution plans strictly as per evaluation matrix to identify the best resolution plan. It is not clear as to why mention of evaluation matrix in sub-regulations 1 through 3 of Regulation 36A was removed while amending Regulation 36A by above Notification dated 3rd July, 2018. It is important to know that Principal Bench of NCLT, Delhi, *vide* its order dated 5th September, 2018, in (IB)-540(PB)/2017 has already declared amended Regulation 36A as *ultra vires* of Section 240(1) of the Code as it envisages the procedure to be followed through "Expression of Interest" (EOI). It is equally pertinent to state that in W.P.(C) 10189/2018 filed by Insolvency & Bankruptcy Board of India (IBBI), Hon'ble Delhi High Court has stayed the said order by way of an interim order.

CoC is further required to appoint resolution professionals in a timely manner, as provided in Section 22(2) of the Code. In compliance with the requirements of Circular No. IBBI/ CIRP/016/2018 dated 10th August, 2018, issued by IBBI, the interim resolution professional or the resolution professional, as the case may be, has to inform in every notice of meeting of the CoC and any other communication addressed to FCs, other than creditors u/s. 21(6A)(b), that they must be represented in the CoC or in any meeting of CoC by such persons who are competent and authorized to take decisions on the spot, without deferring decisions for want of any internal approval from the financial creditors.

RIGHTS AND PRIVILEGES OF FCs

As is evident, FCs play a pivotal role under IBC, steering the course of corporate debtors and safeguarding the interest of all parties concerned, including their own, within the ambit of the Code. The core object of IBC is maximisation of value of assets and attempts are to ensure that the creditors of a beleaguered corporate debtor enjoy the benefit thereof. FCs, especially lenders dealing with public money, must ensure that they are able to salvage the highest possible amount through a palatable and credible resolution plan and may therefore not desist from placing certain conditions in a resolution plan towards the said purpose. As an example, FCs may explore the possibility of imposing conditions that besides the settlement amount to be received by them under the resolution plan, any monies recovered by the successful resolution applicant either from bad and doubtful receivables or under applications filed by the RP/liquidator in respect of avoidance transactions shall be paid to the credit of FCs or, they may stipulate that personal guarantees or corporate guarantees shall not stand released on approval of a resolution plan. Reference is invited to the matter of *Abhishek Corporation Ltd.*, where the resolution applicant was required at the instance of some banks to delete the clause relating to release of personal guarantees in the resolution plan to be considered by CoC for its approval or otherwise. The examples cited are only illustrative and not exhaustive.

FCs further have a right to receive from the resolution professional a report on avoidance transactions under Sections 43, 45, 49 and 66 of the Code in terms of Regulation 39(2) of the IBBI (Insolvency Resolution for Corporate Persons) Regulations, 2016. It is implicit that FCs are expected to know the affairs of the corporate debtor more intimately and can direct appropriate action to be taken against them to bring culprits to justice.

The erstwhile Regulation 38(1) of IBBI (Insolvency Resolution for Corporate Persons) Regulations, 2016, required the resolution plan to provide for liquidation value due to dissenting FCs, payment of which was to be made before any recoveries are made by FCs who voted in favour of the resolution plan. NCLAT, by its order in Appeal No. 526/2018 in the matter of *Central Bank of India vs. Sirpur Paper Mills* held that Clauses (b) and (c) of Regulation 38(1) being inconsistent with the provisions of the Code, and the legislators having not made any discrimination between the same set of group such as 'Financial Creditor' or 'Operational Creditor', IBBI by its Regulation cannot mandate that the Resolution Plan should provide liquidation value to the 'Operational Creditors' [clause (b) of regulation 38(1)] or liquidation value to the dissenting Financial Creditors [clause (c) of regulation 38(1)]. Such regulation being against Section 240(1) of the Code, cannot be taken into consideration and any Resolution Plan which provides liquidation value to the 'Operational Creditor(s)' or liquidation value to the dissenting 'Financial Creditor(s)' in view of clauses (b) and (c) of Regulation 38(1), without any other reason to discriminate between two sets of creditors similarly situated such as 'Financial Creditors' or the 'Operational Creditors' cannot be approved being illegal. Pursuant to the said judgment of NCLAT, this regulation has been modified by Notification No. IBBI/2018-19/GN/REG032, dated 5th October, 2018, which only states that the amount due to the operational creditors under a resolution plan shall be given priority in payment over financial creditors.

Lastly, Section 28 of IBC confers corresponding rights, privileges and obligations on CoC, with the approval of the majority being a condition precedent for the RP's future course of action. The rights and privileges enjoyed by FCs come with their own set of limitations. To illustrate, under the erstwhile provisions of SICA, 1985, the consent of every bank and public financial institution u/s. 19(2) of the said Act was a condition precedent for sanctioning a scheme, without which BIFR was severely restricted in its ability to do so. SICA therefore provided an uninhibited opportunity to FCs to take decisions which would protect their own interest in the process of rehabilitation of a sick industrial company. Under the Code, this vital aspect is amiss as the decision of FCs comprising 66% or more of the voting share is made binding on all dissenting/residual FCs and other stakeholders, although this vindicates the principle of corporate democracy laid down by the apex court in the matter of Administrator of the Specified Undertaking of the *UTI vs. Garware Polyester Ltd [AIR 2005 SC 2520],* where the Hon'ble Supreme Court had thus held:

"... Once it is held that the normal rule, namely, the principle of majority in corporate democracy or in other words, governance of the company by majority, is accepted, the appellant could not be heard to say that they had an absolute right to exercise veto power and thereby scuttle a bona fide attempt to revive a company. Efforts to keep a company from becoming insolvent and even to revive an insolvent corporate have been receiving legislative and executive support, as would be evident from several Parliamentary Acts, as for example the Sick Industrial Companies (Special Provisions) Act, 1985 and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002."

It is obvious that the time-honoured dictum that majority is the authority has served as a guiding rule in couching Section 30(4) of the Code.

Further, if one takes the instance of contributing towards the CIRP cost, no right appears to have been made available to individual FCs to decide the same as they are expected to fall in line with the majority decision of CoC, which in terms of Section 21(8) of the Code, is 66% or more of the voting share. This is also borne out by the latest order of NCLT, Mumbai, in the matter of *Shanaya Fashions vs. Zephyr Fabrics Trading LLP.*

One may be dismayed to note the judgment of NCLAT in the matter of *Essar Steel Ltd (supra),* where NCLAT changed the pattern of distribution to FCs by allowing payment of 100% to operational creditors and FCs who had to recover less than ₹ 1 crore and ₹ 10 lakh respectively, while revising substantially downward to 60% the amount payable to secured FCs, evidently on the basis of Section 30(2)(b) of the Code, which states the operational creditors should not be paid less than the liquidation value under a resolution plan. The justification advanced in favour of higher payment than liquidation value is that operational creditors have supplied goods or rendered service to the corporate debtor on credit and if they are discriminated, the objective of promoting availability of credit will be defeated. As stated earlier, this judgment has been assailed before the apex court by secured creditors. Another notable finding rendered by NCLAT in the said verdict in the matter of Essar Steel is that once the debt payable by the 'Corporate Debtor' stands cleared in view of the approval of the plan by making payment in favour of the lenders ('Financial Creditors'), the effect of 'Deed of Guarantee' comes to an end as the debt stands paid. The guarantee having become ineffective in view of payment of debt by way of resolution to the original lenders ('Financial Creditors'), the question of right of subrogation of the Appellant's right under Section 140 of the Contract Act and the right to be indemnified under Section 145 of the Contract Act does not arise. It remains to be tested in law whether the guarantor can still stand relieved of his personal guarantee notwithstanding the fact that after adjusting the amount recovered under the approved resolution plan, the balance amount remains to be recovered, given that in most of the cases, the personal guarantee is co-extensive with that of principal debtor. In *Bank of Bihar vs. Damodar Prasad and Anr (1969) 1 SCR 620,* the Hon'ble Supreme Court held that u/s. 128 of the Indian Contract Act, save as provided in the contract, the liability of the surety is co-extensive with that of the principal debtor. The surety thus becomes liable to pay the entire amount and his liability is immediate and not deferred until the creditor exhausts his remedies against the principal debtor.

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Home Buyers under the IBC

Prem Rajani & Aradhana Bhansali,
Advocates

It would not be entirely out of place to state that Insolvency and Bankruptcy Code, 2016 ("**IBC**") has proved to be a '*messiah*' of sorts in trying to resolve the problem of mounted debts and NPAs. The enactment has opened flood gates for issues which obviously are not entirely new and are being tackled before various judicial forums. It surely will pave the way for financial discipline by instilling the much needed assurance to the creditors and bankers by laying down a robust framework for resolution of debts or for liquidation.

Recently, the IBC received a booster shot when, in *Swiss Ribbons Pvt. Ltd. & Anr. vs. UOI*[1], the constitutional validity of IBC was upheld. Within a short span, IBC has already been hailed as one of the revolutionary economic legislations of India, and one really hopes that IBC proves to be a harbinger of better economic prospects. Having said so, the IBC did have its fair share of controversies and criticisms since its enactment. But the law is still evolving and the IBC by itself may not prove to be an all-encompassing panacea for bad loan bug. It can though be safely anticipated that, going forward, the 'creases' would certainly be further ironed out, albeit not entirely, which would only justify the initial promise it has emanated.

One of the recent IBC debates has been the shelter to be given to the homebuyers by regarding them as "financial creditors" so as to enable homebuyers to participate, by becoming part of Committee of Creditors ("**CoC**"), and getting an opportunity to vote on resolution plans of the debtor developer company, who has defaulted in handing over possession of the flats to such homebuyers. Such categorisation of home buyers as financial creditors has come through because of a lot of hue and cry on their part, who are generally left at the mercy of the developers and in some cases, the developers have duped the homebuyers for no fault of theirs. There were and are still several instances where the developers have raised funds from the home buyers and diverted the same or used the funds for some other project or diverted it for some alien purposes to suit their desires. This issue, being of a very sensitive nature, has garnered tremendous debate at judicial forums along with the media glare. Cases of *Jaypee* and *Amrapali* considered the miserable plight of the home buyers who were earlier not recognised as Financial Creditors.

1. *Swiss Ribbons Pvt. Ltd. & Anr.* vs. *UOI*- Writ Petition (Civil) No. 99 of 2018

Since homebuyers were not capable of initiating insolvency proceedings against defaulting builders, the Insolvency and Bankruptcy Amendment Bill (Second Amendment), 2018 was passed to treat homebuyers as "financial creditors" due to which homebuyers heaved some sigh of relief.

It is worth mentioning that the very year (2016, when IBC was enacted), another statute, Real Estate (Regulation and Development) Act, 2016 ("**RERA**") also came into force, which is equally a powerful legislation enacted for the sole objective to streamline the real estate sector which traditionally has worked more on the whims and fancies of the developer. RERA provides the regulatory framework for the real estate sector, including promoting the welfare and protecting the interests of the homebuyers, and has been long desired to instil some discipline in the developers with a view to inspire the confidence of the homebuyers and the investors alike.

Originally, IBC did not have any specific relief for homebuyers and as such it was felt that they were being left in lurch.

The fourth estate has really been active informing public at large regarding the unscrupulous and dubious activity on the part of developer, who have their grand advertisements splashed over media regarding their projects, where some such developers also play around with the hard-earned money of the buyers. The dreams of such home buyers get totally shattered and all hell breaks lose for them when such large real estate developers default to pay several crores they owe to their bankers/financial institutions; and as such, these lenders, being financial creditors, initiate liquidation proceedings under the IBC. It is considering the recent past, when several home buyers informed the Apex Court about their deplorable state that the Apex Court deemed it fit to include them to participate in the resolution plan of the developer company.

Prior to the said IBC amendment, home buyers were ranked almost at the bottom in the hierarchy of the waterfall mechanism provided under Section 53 of the IBC for recovering their monies they had paid to the developer. Such categorisation had put the home buyers in a limbo, more so due to the recent underperformance of the real estate sector.

Prior to the IBC amendment for homebuyers, the question was whether the home buyers would be regarded as operational creditors or financial creditors? The NCLAT in the case of *Nikhil Mehta vs. AMR Infrastructure*[2], recognised the status of the homebuyer as a financial creditor. The reasoning given by the NCLAT was that the homebuyer under the terms of their specific agreement with the developer, qualified as investors with an assured committed return plan and therefore the amounts paid by the homebuyer in accordance with the sale purchase agreement was treated at par with a loan thereby bringing their investment within the meaning of financial debt. The same reasoning was applied by the NCLAT in the case of *Anil Mahindroo vs. Earth Iconic Infrastructures Ltd*[3].

When IDBI Bank initiated insolvency proceedings in the Jaypee Infra case[4], it left thousands of innocent home buyers in a wobble, since, once the IBC proceedings are initiated, a moratorium

2. NCLAT, New Delhi in case of *Nikhil Mehta and Sons (HUF) & Ors.* vs. *AMR Infrastructure Ltd.,* Company Appellate Jurisdiction, Company Appeal (AT) (Insolvency) No. 07 of 2017, Date of Order: 21-7-2017. (Amended order dated 9-8-2017)
3. *Anil Mahindroo & Another* vs. *Earth Iconic Infrastructures (P) Ltd.* Company Appeal (AT) (Insolvency) No. 74 of 2017
4. *IDBI Bank* vs. *Jaypee Infratech Limited*- CP. No. 77/ALD/2017 and Writ Petition (Civil) No. 744/2017

is declared and other suits filed against such Corporate Debtor would stand abated and the home buyers would not have a recourse for filing new suits due to such a moratorium.

One Chitra Sharma approached the Hon'ble Supreme Court seeking reliefs for such home buyers who were dispossessed with their dream homes and were deprived of any recourse to procure their hard-earned money. At this stage, the home buyers did not form part of the financial creditors and were only eligible to get any returns provided there was any money left after the distribution of the proceeds to other stakeholders. The Supreme Court then came to the rescue of the homebuyers and stayed the insolvency proceedings against Jaypee Infra.

In March 2018, the Insolvency Law Committee Report suggested that the home buyers should be considered as 'financial creditors' and accordingly there was an amendment ordinance which was passed on June 6, 2018, which categorised the home buyers as financial creditors. Pursuant to this amendment, the home buyers were eligible to initiate insolvency proceedings against developers. Prior to this amendment, the options available to home buyers were under the Consumer Protection Act, 1986 ("**CPA**") and thereafter RERA.

Under RERA, home buyers are given an option to either gain possession of the house within a stipulated time period, as per the terms of the agreement between a home buyer and a developer, or to seek refund if there are defaults on the part of a developer. Under CPA, the home buyer would come under the purview of deficiency in service and therefore approached the Consumer Forums for deficiency in service. The result of this IBC amendment was that any amount raised from an allottee under a real estate project was deemed to be an amount having the commercial effect of a borrowing and the expressions 'allottee' and 'real estate' would mean as ascribed to them under RERA.

This amendment *prima facie* seemed like a very sweet deal but upon implementation, did not actually turn out to be likewise. The home buyers are represented by resolution professional in the CoC meetings who have to decide on resolution plans with a holistic approach.

Though, the homebuyer has been reckoned as a financial creditor, the definition of the term 'default' for the purpose of homebuyer has not been revised accordingly. It remains an unanswered question as to when a builder is supposed to have 'defaulted'. The inclusion of home buyers as financial creditor indicates a pre-supposition on part of the builder to have already been defaulted. The reason for delay in possession of flats may not necessarily be due to the default of developer and could also be due to non-payment of consideration by the homebuyer. The IBC amendment presently does not factor this anomaly.

In case of *Ajay Walia vs. M/s. Sunworld Residency Private Limited*[5], the NCLT has come across instances where homebuyers have created third party interests in favour of the banks and have subrogated their rights in favour of the banks. Since the rights have been subrogated tin favour of the banks, they cannot be termed as financial creditors. The action by the homebuyer could also prove to be coercive and as a pressure tactic and the home buyers may get a good settlement deal by threatening the initiation of insolvency proceedings against a financially sound builder, which may force a builder to settle the matter in order to avoid a financially sound and well operational entity to go into liquidation.

5. NCLT Allahabad [*Ajay Walia* vs. *M/s. Sunworld Residency Private Limited*, CP (IB) 11/ALD/2018]

Another big question to be decided is whether the homebuyers would be regarded as secured or unsecured financial creditors.

Meanwhile, several developers have approached the Supreme Court to challenge the inclusion of homebuyers as financial creditors, some citing it as a mode for arm twisting developers. The Apex Court also stayed IBC proceedings initiated by homebuyers against the builders, which include Pioneer Urban Land and Infra, Ansal Homes, Future World Green Homes, Today Homes and Parsavnath Developers.

Many developers have filed petitions challenging Section 5(8) and Section 7 of the IBC, which regard the homebuyers as financial creditors. The developers have contended that the home buyers should not be regarded as financial creditors akin to a bank since the money paid by homebuyers is not in the nature of credit extended by financial lenders. Also, homebuyers are seeking parallel reliefs and cancellation of flats under RERA, refund of money under IBC, the petitions said. The Supreme Court is yet to decide on the constitutionality of Section 5(8) and Section 7 that grants homebuyers the status of financial creditors.

In response to the petitions filed by the developers challenging the inclusion of homebuyers as Financial Creditors, the Centre, recently filed an affidavit in the Apex Court that there was no illegality in amendment brought to the IBC in this respect. The Centre stated that the IBC was amended to protect the interests of lakhs of homebuyers who had invested their hard-earned money to purchase flats but were cheated by companies.

It is pertinent to note that the tool provided to homebuyers needs to be used with utmost caution as it may also be used as a money-making tool by 'unscrupulous homebuyers' which could not only threaten to shake the foundation of a solvent entity but also create doubts about the very basis on which the IBC was amended in the first place to 'placate' the homebuyers. This could be a big blow for genuine buyers and bonafide developers.

The IBC itself is evolving and it remains to be seen whether the Apex Court or any subsequent IBC amendment 'allots' some permanent solution to the homebuyers and calms their jittery nerves or re-starts the entire saga.

The regulatory regime in the country has attempted certain remedy for homebuyers in light of their problems. It seems though the issue is far from resolved. It needs to be seen as to which side has the last laugh, whether the builder or the 'pitiful' home buyer.

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This body is the boat which will carry us to the other shore of the ocean of life. It must be taken care of. Unhealthy persons cannot be Yogis.

– Swami Vivekananda

Always keep your mind joyful; if melancholy thoughts come, kick them out.

– Swami Vivekananda

Bank Guarantees in the context of The Insolvency and Bankruptcy Code, 2016 (IBC)

CA Ajay Joshi

The law on guarantees forms part of the Indian Contract Act 1812 with Section 126 defining guarantees and then there are other sections that cover the rights and liabilities of the creditors and guarantors etc. In the context of IBC, we will restrict ourselves to guarantees for repayment of loans.

A contract of guarantee has three elements; the entity that has borrowed the money (the principal debtor), the entity that has provided the funds (the creditor) and the Guarantor.

The contract of guarantees will have the following features (unless specifically modified):

A. Once entered into the Guarantor cannot walk away from his obligations until the expiry date of the guarantee unless there is anything contrary to that effect in the guarantee document.

B. The liability of the guarantor and the borrower is independent and co-extensive.

C. The creditor can independently proceed against the principal borrower and the guarantor

D. Any modification to the guarantee instrument without the consent of the guarantor can release the guarantor of his obligations.

E. The guarantor will have a right of subrogation i.e., once the guarantor has fulfilled his guarantee obligations, he will have a right to claim the amount from the principal borrower

In the context of IBC, broadly, three types of guarantees are at the centre stage:

A. Personal Guarantees of the Promoter/Directors to Banks etc. for repayment of loans by the corporate debtor

B. Corporate Guarantees given by a Corporate debtor for example, Corporate Guarantee given by a Holding Company for guaranteeing obligations of a subsidiary company.

C. Guarantees issued by Banks upon the request of the corporate debtor

Guarantee as a Debt

The IBC defines Debts as financial debt and operational debt. Operational debt is the amount due to a supplier for provision of goods and services and includes workers and employees' dues, dues owned to the government and others. Sec 5 of the IBC has an exhaustive list of what constitutes financial debt with guarantees covered under clause 8 subclause (i) which reads as:

"the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub clauses referred to in sub clauses (a) to (h) of this clause."

The treatment of guarantees under IBC has seen many issues emerge as under:

A. Whether uninvoked guarantees can be admitted as a debt

The position taken by some RPs was that unless a guarantee has been invoked, it does not become a debt. The guarantee may lapse and therefore only when the guarantee has been invoked can that be admitted as a debt and the beneficiary of the guarantee treated as a Financial Creditor. (The article is in the context of financial guarantees only). Another position taken by an RP, *inter alia*, was that for a guarantee to be treated as a financial debt, the guarantee must have been issued by a financial institution, in terms of IBC, and therefore if a Corporate Guarantee for a loan has been given then the guarantee cannot be treated as a financial debt. In many cases though, RPs have admitted uninvoked guarantees as a valid claim. It is the view of this author that the obligation of the guarantor is absolute under law. The guarantor therefore has a stake in the process and if anytime the guarantee gets invoked then there is no difference between the creditors who have extended loans and say a bank that has issued a guarantee on behalf of a corporate debtor. The guarantor cannot be denied a seat on the Committee of Creditors only because the guarantee has not been invoked. Further sub-clause 8 (i) only provides for guarantees and there is no distinction between Invoked and Uninvoked Guarantees.

This matter came to be heard by the Hon'ble NCLAT in the case of *Axis Bank vs. Edu Smart Services Private Limited and others* in Corporate debtor Appeal (AT) 304 of 2017. Prior to the filing of the appeal in NCLAT, the Hon'ble Principal Bench of NCLT at New Delhi rejected the claim of Axis Bank stating that as of the date of admission under CIRP, the claim was contingent as the guarantee had not been invoked. It also concurred with the views of the RP in the case that the moratorium under Section 14 does not permit invocation of a guarantee once the corporate debtor has been admitted under CIRP. The CoC in this case also claimed that claim for unmatured debt under a guarantee cannot be accepted as the debt has not become due and payable.

The Hon'ble NCLAT differentiated between claim and default. It was held that the claim as defined under Section 3(6) of the Code means, *inter alia*, right to payment and for any application for Insolvency to be triggered, default must have take place and default as defined under Section 3(12) of the IBC reads as "default means non payment of debt when.........debt has become due and payable".

The Appellate Tribunal held that when the Insolvency has been triggered then everyone who has a right to payment can file a claim with the IRP/RP and that the claim has not matured cannot be a ground for rejection of the claim.

The Hon'ble Appellate Tribunal ruled that

"Therefore, we hold that maturity of claim or default of claim or invocation of guarantee for claiming the amount has no nexus with filing of claim pursuant to public announcement made under Section 13(1)(b) r/w Section 15(1)(c) or for collating the claim under Section 18(1)(b) or for updating claim under Section 25(2)(e). For the purpose of collating information relating to assets, finances and operations of Corporate Debtor or financial position of the Corporate Debtor, including the liabilities as on the date of initiation of the Resolution Process as per Section 18(1), it is the duty of the Resolution Professional to collate all the claims and to verify the same from the records of assets and liabilities maintained by the Corporate Debtor."

Further it was also held that the Guarantee need not be issued only by a financial institution and by implication that creditors issuing Corporate Guarantees shall also be treated as a financial debt.

There would, however, be a practical issue that would emerge at the time distribution under the approved resolution plan when the guarantees have not been invoked. In principle, if the guarantee has not been invoked at the time of distribution then the creditor cannot get the benefit of the payment against uninvoked guarantees.

The following scenarios are most likely:

A. Both, the primary and claim period under the guarantees have expired

B. The primary period has expired but the claim period is still valid

C. The primary and the claim period are valid as of the date of the planned distribution.

D. The Guarantee has been invoked and payout has been made by the creditor

It is also a fact that in many cases, some of the guarantees may have been issued to power companies, utilities supplying water etc. and the continuation of these guarantees would be essential to maintain operations of the corporate debtor.

The probable treatment for the uninvoked guarantees would be as under:

A. As far as A above is concerned, since the Creditor has no further liability to honour the guarantee, his claim amount will need to be reduced.

B. In the case of B above, from the total share due to the Creditor, the amount payable if invocation was to happen will be held back and not distributed till the claim period has expired. If invocation happens then the creditor will receive the portion of the plan distribution against the claim admitted and if there is no invocation then the amount will need to be redistributed to all the creditors unless the approved resolution plan has specifically provided that in the event of non invocation, the successful resolution applicant will reduce the total amount that it has agreed to pay under the resolution plan against the guarantee claim.

C. In the case of C above, it is possible that the Resolution Applicants will need to carry forward the guarantees and get these renewed or substituted by new guarantees. This is likely where guarantees are issued to Utilities Companies or for Contracts under execution and similar purposes. In such a scenario, if these guarantees are being taken over by the resolution applicants then the creditor will need to reduce their claim and the distribution pattern would be worked out with the change in the admitted claim. If, however, the guarantees are not being taken over by the successful Resolution Applicants then the same treatment under B will be followed and the payout in relation to the guarantees will happen only after the eventual fate of the guarantees is known.

D. Of course, if the guarantees have been invoked and payout has happened then the guarantee will be a part of the total admitted claim and the creditor shall receive the payout as agreed under the resolution plan against that admitted claim at the time of settlement.

As the readers might have noticed, that in the cited case, NCLAT did not rule on whether guarantees can be invoked during the moratorium period under Section 14 of the IBC. Prior to the amendment brought about in the IBC on 6th June 2018 through the The Insolvency and Bankruptcy Code (Second Amendment) Act, 2018, there have been judgments that have ruled that the guarantees cannot be invoked during the moratorium period. However the amendment to the Act inserted in sub-section 3 under which in clause (b) it is specified that

"The provision of sub-section (1) shall not apply to a surety in a contract of guarantee to a corporate debtor".

Accordingly, it appears that post the amendment there is no restriction on a beneficiary of the guarantee to invoke and get paid the guarantee amount during the moratorium period. In the case of *Levcon Valves Private Limited vs. Energo Engineering Projects Limited* the Hon'ble NCLAT in its judgment has held that Performance Guarantee issued by Banks can be invoked during the moratorium period. The Hon'ble Supreme Court in the matter of *State Bank of India vs. V. Ramakrishnan and Others* has also ruled that there is no bar on the invocation of personal guarantees during the moratorium period under Section 14 of the IBC.

Obligations of the Guarantor and Corporate Debtor

As discussed earlier, under the Contract Act, the obligations of a Guarantor and Borrower are co-extensive and independent. The main question that has arisen in the past is that if a financial creditor has already commenced Insolvency Proceedings against the Corporate Debtor, can the same creditor also initiate Insolvency Proceedings against the guarantor.

Another question conversely is that can the creditor proceed against the guarantor without first moving against the Corporate Debtor (principal debtor).

This matter came up for examination by the Hon'ble NCLAT in the case of *Vishnu Kumar Aggarwal vs. Piramal Enterprises.* The Hon'ble NCLAT ruled that there is no requirement that the financial creditor must first proceed against the principal borrower and then only against the guarantor. The order ruled that the liability of the guarantor is co-extensive with the borrower and the guarantor is a debtor *qua* the financial creditor. The Appellate Authority also relied on two Supreme Court judgments in the cases of *Bank of Bihar vs. Damodar Prasad & Anr* and State *Bank of India vs. Indexport Registered and Ors.* Accordingly, a financial creditor can proceed simultaneously against the Corporate Debtor and the Guarantor and also independently against the guarantors without proceeding against the borrower. This position was further affirmed by the Hon'ble Supreme Court in the matter of an appeal filed by Raj Bahadur Shree Ram and Corporate Debtor Private Limited against the decision of the Hon'ble NCLAT in the matter of *Ferro Alloys Corporation vs. Rural Electrification Corporation Limited.*

As stated earlier in this paper, there is no bar in invoking the personal guarantee during the moratorium period. The invocation proceedings, currently, are dealt in the Debt Recovery Tribunal (DRT) and even under the IBC, once Part III on Insolvency of Individuals and Partnership Firms is notified, DRT is the designated authority. The Hon'ble NCLAT in its order in the case of *State Bank of India vs. D. S. Rajkumar* has ruled that while the Part III is yet to be notified, under Section 60(2) of the IBC, it is open for the financial creditor to initiate Insolvency Resolution Process against corporate and personal guarantors and such proceeding are to be filed with the same NCLT where the Insolvency Resolution Process against the corporate debtor has been filed. It will be noted that unlike the case where an application can be filed independently against the guarantor without proceeding against the Corporate Debtor, under Section 60(2) of IBC, insolvency proceeding must have been filed against the Corporate Debtor. It can thus be summarised that while in case of corporate guarantee application can be filed under Section 7 of the IBC by a financial creditor, for an insolvency or bankruptcy proceeding against a personal guarantor, insolvency proceeding against the corporate debtor must have commenced in NCLT.

Right of Subrogation

Section 140 of the Contract Act provides that once the guarantor has honoured its obligations under the guarantee, he is invested with the all the rights that the creditor had against the principal debtor. This is also called the Right of Subrogation. Section 133 of the Contract Act also provides for discharge of the surety by variance in the terms of the contract between the principal debtor and the creditor without the consent of the guarantor. Generally, though, in case of loans provided by the financial creditors, sufficient rights are provided to the financial creditor for changes to the loan amount, variation in the loan conditions etc. as a part of the guarantee contract. Each creditor will normally sign an independent contract with the guarantor.

In the past. litigation has taken place as to whether the resolution applicants can provide that the guarantors shall not have a right of subrogation against the corporate debtor or the resolution applicants.

The matter of right of subrogation came for consideration of the Hon'ble NCLAT in the matter of *Lalit Mishra and Ors vs. Sharon Bio Medicine*. In this case, the resolution plan provided that personal guarantees provided by the existing promoters of the corporate debtor shall result in no liability towards the corporate debtor or the resolution appellants. It was alleged by the appellants that this clause was in contravention to Section 133 and Section 140 of the Contract Act.

The Hon'ble NCLAT ruled that

"However, the aforesaid submissions cannot be accepted, as on approval of the 'Resolution Plan', the claim of the entire stakeholders stand cleared and the 'Personal Guarantor' thereafter cannot claim that they have been discriminated. All the stakeholders have already been cleared by the 3rd Respondent- 'Successful Resolution Applicant'. It was open to them to say that the personal guarantee will not result into any liability towards the 'Corporate debtor' or the 'Resolution Applicant'.

9. It was not the intention of the legislature to benefit the 'Personal Guarantors' by excluding exercise of legal remedies available in law by the creditors, to recover legitimate dues by enforcing the personal guarantees, which are independent contracts. It is a settled position of law that the liabilities of guarantors is co-extensive with the borrower. This Appellate Tribunal held that the resolution under the 'I&B Code' is not a recovery suit. The object of the 'I&B Code' is, inter alia, maximization of the value of the assets of the 'Corporate Debtor', then to balance all the creditors and make availability of credit and for promotion of entrepreneurship of the 'Corporate Debtor'. While considering the 'Resolution Plan', the creditors focus on resolution of the borrower 'Corporate Debtor', in line with the spirit of the 'I&B Code'.

10. The present appeal has been preferred by the promoters, who are responsible for having contributed to the insolvency of the 'Corporate Debtor'. The 'I&B Code' prohibits the promoters from gaining, directly or indirectly, control of the 'Corporate Debtor', or benefiting from the 'Corporate Insolvency Resolution Process' or its outcome. The 'I&B Code' seeks to protect creditors of the 'Corporate Debtor' by preventing promoters from rewarding themselves at the expense of creditors and undermining the insolvency processes."

Accordingly, this now seems to be settled law as it is not known whether this judgment has been appealed against.

Validity of Promoter Guarantees when debt is extinguished/settled

A resolution plan may provide for that either the entire financial debt is fully settled or may provide that the existing lenders will assign the debt in favour of the resolution applicants. While in the first case, no debt remains in the books of the lenders as well as the Corporate Debtor, in the second case the resolution applicants step into the shoes of the financial creditors and the debt remains in the books of the Corporate Debtor. Under both the situations, as far as Guarantees are concerned, either these would remain with the financial creditors or assigned to the resolution applicants.

There has been an argument that when there is no debt outstanding in the books of the financial creditors arising out of an approved resolution plan then on what basis the creditors can invoke the promoter guarantees. The guarantee is for repayment of the loan by the principal debtor to the creditor but when there is no debt left in the books of the creditor that implies that the debt has been repaid and therefore the guarantor can argue that it is no longer liable under the contract of guarantee. There does not seem to be a specific provision for such a situation under the Contract Act and the legal position on this point was not settled until the is not yet settled latest judgment in the matter of *Standard Chartered Bank vs. RP of Essar Steels Limited & Ors.,* Corporate debtor Appeal (AT) (Ins.) No. 242 of 2019.

The Hon'ble NCLAT has ruled that once the debt is satisfied then the creditor cannot proceed against the guarantors. The Hon'ble Tribunal under Para 30 and 31 of the said Judgment stated that

"30. So far as the Appellant- Mr. Prashant Ruia's right of subrogration under Section 140 of the Contract Act and right to be indemnified under Section 145 of the said Act is concerned, the question of exercising such right does not arise in the present case.

31. The Appellant- Mr. Prashant Ruia has executed a 'Deed of Guarantee' between the lenders and the 'Corporate Debtor'. Such guarantee is with regard to clearance of debt. Once the debt payable by the 'Corporate Debtor' stands cleared in view of the approval of the plan by making payment in favour of the lenders ('Financial Creditors'), the effect of 'Deed of Guarantee' comes to an end as the debt stands paid. The guarantee having become ineffective in view of payment of debt by way of resolution to the original lenders ('Financial Creditors'), the question of right of subrogation of the Appellant's right under Section 140 of the Contract Act and the right to be indemnified under Section 145 of the Contract Act does not arise."

Again in Para 221 of the said judgment, the Hon'ble NCLAT has ruled that

"The 'Financial Creditors' in whose favour guarantee were executed as their total claim stands satisfied to the extent of the guarantee, they cannot reagitate such claim from the Principal Borrower"

Accordingly, it appears that the latest position in law is that once the debt is settled *qua* the financial creditors, the guarantee obligation ceases and consequently Section 140 and Section 145 of the Contract Act are also not applicable under an approved Resolution Plan. It is understood that the Committee of Creditors has approached the Hon'ble Supreme Court in appeal against the above judgment covering *inter alia*, the ruling on the personal guarantee. It is expected that the law on guarantees under IBC will also be settled once the judgment has been delivered.

Disclaimer

The above discussion is not a legal opinion or a detailed legal exposition on the issue of Guarantees. Accordingly, the readers are advised to consult their legal counsel for any specific issue. The purpose of this Article is to provide a broad understanding of the issues that have been raised and settled by the Courts.

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Powers and Duties of Board Members under IBC

Makarand Joshi & Kumudini Paranjape
Company Secretaries

Introduction

Insolvency and Bankruptcy Code, 2016 ("IBC 2016")was enacted on 28th May 2016 to consolidate and amend laws relating to re-organisation, insolvency, to develop entrepreneurship, protect interest of all stakeholders and establish Insolvency and Bankruptcy Board of India etc.

The intent is to find out resolution for sick business with the help of battery of professionals and healthy acquirers. The shift of approach from debtors to creditors and attempting to find resolution in time bound manner has cast duties and responsibilities on the Resolution Professional who is appointed. But nonetheless, the Board of Directors of the Corporate Debtor is duty bound to assist, help the Resolution Professional or Creditors in the best interest of all stakeholders.

Section 17 of IBC 2016 (Suspension of Powers of the Board of Directors)

We all know that as per section 17(1)(b) of the IBC 2016, the powers of the Board of Directors or the partners of corporate debtor, stands suspended and exercised by the interim resolution professional. As per Section 17(1)(c), the officers and managers of the corporate debtor shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional.

As per Section 17(2) of the IBC 2016, the Interim Resolution Professional is vested with the management of corporate debtor.

As per Section 19(1) of the IBC 2016, the "personnel" of corporate debtor, its promoters or any other person associated with the management of corporate debtor shall extend all assistance and co-operation to the IRP as may be required by him in managing the affairs of the corporate debtor.

Though the powers of the board of Directors of the Corporate Debtor are suspended as per section 17 of the IBC 2016, still they are duty bound to provide all assistance as per section 19 of the IBC 2016.

Further, the Corporate Debtor is managed to operate as going concern by the IRP. Hence, all other Acts, Rules, Regulations etc. are applicable unless specifically exempt under the IBC 2016.

Duties of Directors under the Companies Act, 2013

Section 166 of the Companies Act, 2013 provide for duties of Directors.

The management of a Company is entrusted to a body of persons called "directors". Enormous cases have dwelt upon the position of directors. However, the true position of directors is that they are in fiduciary relationship with the Company. It is sufficient to say that the directors occupy a fiduciary position and all the powers entrusted to them are only exercisable in this fiduciary capacity[1].

The term "fiduciary" is derived from the Roman law and it means a person who is required to act for the benefit of another person on all the matter within the scope of their relationship; one who owes to another the duties of good faith, trust, confidence and one must exercise a high standard of care in managing another's money or property.

The fiduciary capacity within which directors have to act ***enjoins upon them a duty to act on behalf of the company with utmost care and skill and due diligence and in the interest of the company*** *The directors are not entitled to use their powers merely for the purpose of maintaining their control over the affairs of the company or merely for their extraneous purposes to benefit themselves. The directors have a duty to make full and honest disclosure regarding all important matters relating to the company. The acts of directors in a private limited company are required* ***to be tested on a much finer scale in order to rule out any misuse of power*** *for personal gains or ulterior motives*[2].

Section 166 of the Companies Act, 2013 – Duties of the Directors:

(1) Subject to the provisions of this Act, a director of a company shall act in accordance with the articles of the company.

(2) A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.

(3) A director of a company shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.

(4) A director of a company shall not involve in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company.

(5) A director of a company shall not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates and if such director is found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company.

(6) A director of a company shall not assign his office and any assignment so made shall be void.

(7) If a director of the company contravenes the provisions of this section such director shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

Judgment highlighting duties and fiduciary role of director under IBC, 2016

Apart from the duties mentioned under the Companies Act, 2013 and Section 19 of the

1. Palmar 's Company Law, 23rd ed., p 838
2. *Shri Kultar Sehgal And Ms. Manprit ... vs. Broadvision Digital Prints (I)* ... on 23 March, 2007

IBC, 2016, there are various judgments which highlight the duties and fiduciary role of directors during the resolution process.

The Board of Director is entrusted with the power to run the business of the Company in the best interest of various stakeholders. ***The order passed by NCLAT in the case of M/s. Subasri Realty Private Limited strengthens*** *this view by stating that after appointment of the Resolution Professional and declaration of moratorium, the Board of Directors stands suspended, but that does not amount to suspension of Managing Director or any of the Director or officer or employee of the Corporate Debtor. To ensure that the Corporate Debtor remains on going concern, all the Director/ employees are required to function and to assist the Resolution Professional who manages the affairs of the Corporate Debtor during the period of moratorium.*

Further, whether the Board has a power to attend meeting of Committee of Creditors or whether they can get copy of resolution plan? All such questions are answered by the judgments in recent times. Few of the questions are listed below:-

Whether the Board of Directors have the right to attend the meeting of the Committee of Creditors?

As per section 24 of the Code, the Board of Directors have the right to attend the meeting of Committee of creditors, however they don't have right of voting.

Whether the Board of Directors have the right to get the copies of Resolution Plan?

The Supreme Court in the case of *Vijay Kumar Jain vs. Standard Chartered Bank and others,* 2019 SCC online SC 103 dealt with the issue as to whether the resolution professional should provide all the documents including the insolvency resolution plans to the suspended board of directors of the corporate debtor.

On a combined reading of the Code as well as the Regulations, the Supreme Court held that members of the erstwhile Board of Directors, being vitally interested in resolution plans that may be discussed at meetings of the Committee of Creditors, must be given a copy of such plans as part of "documents" that have to be furnished along with the notice of such meetings.

Failure to perform duties by Board of Directors

What if the Directors fail to perform their duties as per Section 19 of the IBC 2016:–

The management affairs of the Company are executed and operated by the RP. However, the directors suspended are required to extend all assistance and cooperation to the RP to enable him to manage the affairs of the corporate debtor. On failure to extend all the assistance, the management/personnel shall be liable u/s. 70 of the IBC 2016 for imprisonment which may be 3 years and may extend to 5 years or fine which shall be not less than one lakh rupees and which may extend to one crore rupees or with both[3]. There are other penalties too.

Preference and Undervalued Transactions

If the Company has given any preference to a property or an interest of the company has been transferred for the benefit of a creditor or a surety or a guarantor for or on account of an ancestor financial debt or operational debt or other liabilities owed by the corporate debtor and putting such creditor or surety or guarantor in a position which is more beneficial to him, than it is treated as the case of distribution of preference transactions.

3. In the matter of *M/s Educomp Infrastructure & School Management Limited vs. Mr. Ashwini Mehra,* Resolution Professional.

As per Section 48 read with Section 45, Section 46 and Section 43, if during the CIRP process, RP examines that the corporate debtor has entered into transactions which were undervalued or any preferential treatment is given, it shall inform the adjudicating authority. Adjudicating authority in case of such applications shall make an order to declare the transaction void OR reverse the effect of such transactions.

The relevant period considered for review of preference/undervalued transaction is –

- 12 months for regular transactions and
- 24 months for related party transactions

Fraudulent trading or wrongful trading

Section 66 provides that the directors exercise reasonable due diligence for any function carried out by them in order to minimize the potential loss to creditors of the company. If during the CIRP process RP found that the business of the Company has been carried out to defraud its creditors or for any fraudulent purpose and if the directors were knowingly parties to the carrying on of the business in such manner OR it is found that the directors:

a) before the insolvency commencement date knew or ought to have known that the there was no reasonable prospect of avoiding the commencement of a corporate insolvency resolution process in respect of such corporate debtor; and

b) such director or partner did not exercise due diligence in minimizing the potential loss to the creditors of the corporate debtor

Then, Adjudicating Authority on an application made by the RP may by an order direct that shall contribute to the assets of the Company ie., make him personally liable.

Conclusion

The IRP takes over the management as the going concern. The IRP takes each and every endeavour to protect and preserve the value of the property of the company and manage the operations of the corporate debtor as a going concern. The directors are required to assist the IRP in each and every step to make the process smooth and hailing as stated under section 19 of the IBC 2019 though their powers are suspended as per Section 17(1)(b) of the IBC 2016.

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Be brave, be brave! Man dies but once. My disciples must not be cowards.

– *Swami Vivekananda*

Arise, awake and stop not till the desired end is reached. Be not afraid, for all grate power, throughout the history of humanity, has been with the people. From out of their ranks have come all the greatest geniuses of the world.

– *Swami Vivekananda*

Recent judgments on compromise and arrangements at the stage of liquidation under the IBC

Ashish Pyasi
Advocate

"What is interesting to note is that the ***Preamble does not, in any manner, refer to liquidation which is only availed of as a 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 **Hon'ble Supreme Court in Swiss Ribbons**

The latest newsletter of the Insolvency and Bankruptcy Board of India suggests that out of 2,162 Corporate Debtors admitted into Corporate Insolvency Resolution Process and 475 Corporate Debtors have ended into liquidation – 445 have already crossed the statutory period of 270 days which would mean that most of them may end up into liquidation.

The Insolvency and Bankruptcy Code, 2016 ("Code") was introduced with the objective "to consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximisation of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues…" and nowhere it suggested for liquidation.

After the introduction of section 29A, the promoters and the suspended board being barred from submitting a resolution plan, the chances of the Corporate Debtors facing liquidation have also increased. In the entire Corporate Insolvency Resolution Process, liquidation should be the last resort and same has been observed by the Hon'ble Supreme Court in the matter of *Swiss Ribbons and Arcelormittal.*

It becomes important that while adjudicating the cases under the Code the objective of the Code must be kept in mind. The Preamble gives an insight into what is sought to be achieved by the Code. The Code is first and foremost, a Code for reorganisation and insolvency resolution of corporate debtors. Unless such reorganisation is effected in a time-bound manner, the value of the assets of such persons will deplete. Therefore, maximisation of value of the assets of such persons so that they are efficiently run as going concerns is another very important objective of the Code. This, in turn, will promote entrepreneurship as the persons in management of the corporate debtor are removed and replaced by entrepreneurs. When, therefore, a resolution plan takes off and the corporate debtor is brought back into the economic mainstream, it is able to repay its debts, which, in turn, enhances the viability of credit in the hands of banks and financial institutions. Above all, ultimately, the interests of all stakeholders are looked after as the corporate debtor itself becomes a beneficiary of the resolution scheme – workers are paid, the creditors in the long run will be repaid in full, and shareholders/investors are able to maximise their investment. Timely resolution of a corporate debtor who is in the red, by an effective legal framework, would go a long way to support the development of credit markets.

The Hon'ble Supreme Court in the matter of Swiss Ribbon has observed that that the primary focus of the legislation is to ensure revival and continuation of the corporate debtor by protecting the corporate debtor from its own management and from a corporate death by liquidation. The Code is thus a beneficial legislation which puts the corporate debtor back on its feet, not being a mere recovery legislation for creditors. The interests of the corporate debtor have, therefore, been bifurcated and separated from that of its promoters/those who are in management. Thus, the resolution process is not adversarial to the corporate debtor but, in fact, protective of its interests.

The resolution process will fail in the event the majority of creditors decides for liquidation, none expresses interest in the corporate debtor, resolution plan is rejected by the Committee of Creditors or the Adjudicating Authority or the approved resolution plan is breached by the corporate debtor. In the aforementioned circumstances, the corporate debtor will go into liquidation. The provisions of the Code does not provide for any reorganisation or scheme of arrangement during the liquidation process. Though the provisions of the Code are silent on the aspect on restructuring however the Regulations provides that the corporate debtor can be sold as a going concern (Regulation 32). With the recent judgments, there is another attempt under Section 230 of the Companies Act to seek revival of the companies facing liquidation.

Jurisprudence on Section 230 of the Companies Act, 2013

The jurisprudence on liquidation process under IBC is evolving into restructuring process under section 230 of the Companies Act, 2013. The provisions of Section 230 under the Companies Act, 2013 is akin to the provisions of section 391 of the Companies Act 1956 wherein a liquidator of a company facing liquidation can submit an application before the National Company Law Tribunal for approval of scheme of arrangement with its creditors and members (where applicable). It is also pertinent to note that the scheme can also be filed by a member, creditor and once the scheme is approved it becomes binding on all the stakeholders.

Though, this process of restructuring has been into existence for quite some time however till recently the importance of this provision has increased after the Code coming into effect as the liquidation is taking place under the Code and there are no provisions under the Code providing for restructuring or revival at the stage of liquidation.

Recently, the Hon'ble National Company Law Appellate Tribunal ("NCLAT") has laid down in series of judgments that pursuant to Section 230 of the Companies Act, 2013 the corporate debtor instead of directly taking into liquidation attempt should be made to see that if any compromise or arrangement can be arrived between the stakeholders. In this background, some of the important judgments which have evolved the restructuring at the stage of liquidation are briefly discussed as follows:

1. S.C. Sekaran vs. Amit Gupta and Ors. (Company Appeal (AT) (Insolvency) Nos. 495 and 496 of 2018) - NCLAT

This is the first judgment by the Hon'ble NCLAT wherein the question as to what step should be taken by the Liquidator during the Liquidation was considered. During the liquidation stage, Liquidator required to take steps to ensure that the company remains a going concern and instead of liquidation and for revival of the 'Corporate Debtor' by taking certain measures.

In this case, the Hon'ble NCLAT referred to what has been held by the Hon'ble Supreme Court in the matter of Swiss Ribbons and Arcelormittal and thereafter proceeded to rely upon and reproduced the judgment of the Hon'ble Supreme Court in *Meghal Homes Pvt. Ltd. vs. Shree Niwas Girni K.K. Samiti & Ors. (2007) 7 SCC 753* as follows:

"33. The argument that Section 391 would not apply to a company which has already been ordered to be wound up, cannot be accepted in view of the language of Section 391(1) of the Act, which speaks of a company which is being wound up. If we substitute the definition in Section 390(a) of the Act, this would mean a company liable to be wound up and which is being wound up. It also does not appear to be necessary to restrict the scope of that provision considering the purpose for which it is enacted, namely, the revival of a company including a company that is liable to be wound up or is being wound up and normally, the attempt must be to ensure that rather than dissolving a company it is allowed to revive. Moreover, Section 391(1)(b) gives a right to the liquidator in the case of a company which is being wound up, to propose a compromise or arrangement with creditors and members indicating that the provision would apply even in a case where an order of winding up has been made and a liquidator had been appointed. Equally, it does not appear to be necessary to go elaborately into the question whether in the case of a company in liquidation, only the official lquidator could propose a compromise or arrangement with the creditors and members as contemplated by Section 391 of the Act or any of the contributories or creditors also can come forward with such an application."

After considering the above, the Hon'ble NCLAT proceeded to hold that in view of the provision of Section 230 and the decision of the Hon'ble Supreme Court in 'Meghal Homes Pvt. Ltd.' and 'Swiss Ribbons Pvt. Ltd.', and directed the Liquidator to proceed in accordance with law. Further, the liquidator was directed to verify claims of all the creditors; take into custody and control of all the assets, property, effects and actionable claims of the corporate debtor, carry on the business of the corporate debtor for its beneficial liquidation etc. as prescribed under Section 35 of the I&B Code. The liquidator will access information under Section 33 and will consolidate the claims under Section 38 and after verification of claims in terms of Section 39 will either admit or reject the claim, as required under Section 40. The Hon'ble NCLAT also directed the liquidator that before taking steps to sell the assets of the corporate debtor, the liquidator will take steps in terms of Section 230 of the Companies Act, 2013 for scheme of arrangement/compromise and thereafter observed that the Adjudicating Authority, if so required, will pass appropriate order. It was held that ***only on failure of revival***, the Adjudicating Authority and the liquidator will first proceed with the sale of company's assets wholly and thereafter, if not possible to sell the company in part and in accordance with law. To comply with the directions given by the Hon'ble NCLAT the Liquidator was given 90 days time to complete the process under Section 230 of the Companies Act.

The above judgment set a precedent in terms of revival of the Company facing liquidation before it finally goes to death under liquidation. Further, it laid down the law that the endeavour should be to revive the company before it goes into liquidation and the liquidator is competent to take such steps including steps under the provisions of Section 230 of the Companies Act, 2013.

2. Y. Shivram Prasad and Ors. vs. S. Dhanapal and Ors. (Company Appeal (AT) (Insolvency) Nos. 224 and 286 of 2018)

In this case, as more than 270 days having passed and in absence of any approved Resolution Plan, the Adjudicating Authority had to pass order of liquidation. In this judgment the law laid down in the matter of *S. C. Sekaran vs. Amit Gupta and Ors. (Company Appeal (AT) (Insolvency) Nos. 495 and 496 of 2018)* was followed and thereafter the Hon'ble NCLAT proceeded to give directions to the liquidator to take steps under Section 230 of the Companies Act.

In this case another question which was considered by the Hon'ble NCLAT was whether another opportunity be given to the promoters to pay the outstanding dues. The Hon'ble NCLAT held that the matter can be settled between the parties and an application(s) under Sections 7 or 9 or 10 can be withdrawn only at three stages:

i. Before admission of application under Sections 7 or 9 or 10.

ii. After settlement if reached by Promoters/ shareholders with the Applicant but before the constitution of the 'Committee of Creditors' in view of decision of the Hon'ble Supreme Court in *Swiss Ribbon Pvt. Ltd. & Anr. vs. Union of India & Ors.*

iii. In terms of Section 12A.

In absence of any settlement, if no withdrawal is made at the aforesaid three stages then Resolution Process continues and if any Resolution Plan which is viable and approved by the Committee of Creditors and then by the Adjudicating Authority, the Company can be saved from liquidation. In this case as the period of 270 days had already expired and no approved resolution plan was available, the Adjudicating Authority passed an order for liquidation. In these circumstances the Hon'ble NCLAT proceeded to consider the issue as what steps should be taken by the liquidator during the liquidation.

After considering all the contentions, the Hon'ble NCLAT held that during the liquidation process, step required to be taken for its revival and continuance of the Corporate Debtor by protecting the Corporate Debtor from its management and from a death by liquidation. Thus, the steps which are required to be taken are as follows:

i. By compromise or arrangement with the creditors, or class of creditors or members or class of members in terms of Section 230 of the Companies Act, 2013.

ii. On failure, the liquidator is required to take steps to sell the business of the Corporate Debtor as going concern in its totality along with the employees.

The Hon'ble NCLAT observed that *the last stage will be death of the Corporate Debtor by liquidation, which should be avoided.*

The Hon'ble NCLAT also observed that during proceeding under Section 230, if any, objection is raised, it is open to the Adjudicating Authority (National Company Law Tribunal) which has power to pass order under Section 230 to overrule the objections, if the arrangement and scheme is beneficial for revival of the 'Corporate Debtor' (Company). While passing such order, the Adjudicating Authority is to play dual role, one as the Adjudicating Authority in the matter of liquidation and other as a Tribunal for passing order under Section 230 of the Companies Act, 2013. *As the liquidation so taken up under the I&B Code, the arrangement of scheme should be in consonance with the statement and object of the 'I&B Code'. Meaning thereby, the scheme must ensure maximisation of the assets of the 'Corporate Debtor' and balance the stakeholders* such as, the 'Financial Creditors', 'Operational Creditors', 'Secured Creditors' and 'Unsecured Creditors' without any discrimination. Before approval of an arrangement or Scheme, the Adjudicating Authority (National Company Law Tribunal) should follow the same principle and should allow the liquidator' to constitute a Committee of Creditors for its opinion to find out whether the arrangement of Scheme is viable, feasible and having appropriate financial matrix. It will be open for the Adjudicating Authority as a Tribunal to approve the arrangement or Scheme in spite of some irrelevant objections as may be raised by one or other creditor or member keeping in mind the object of the Insolvency and Bankruptcy Code, 2016.

3. *Rasiklal S. Mardia vs. Amar Dye Chem Limited (Company Appeal (AT) (Insolvency) No. 337 of 2018) - NCLAT*

In this case, the question considered by the Hon'ble NCLAT was whether the shareholder can file an application for scheme of arrangement/compromise. In this case, the National Company Law Tribunal had rejected the application for scheme of arrangement on the ground that the company is under liquidation and therefore the shareholder has no locus and only the Official Liquidator could have filed an application for scheme of arrangement/compromise.

The Hon'ble NCLAT after considering various judgments of the Apex Court and the High Courts held that liquidator is only an additional person and not exclusive person who can move application under Section 391 of the old Act when the company is in liquidation.

4. *Superna Dhawan & Ors. vs. Bharti Defence and Infrastructure Ltd. (Company Appeal (AT) (Insolvency) No. 195 of 2019) – NCLAT*

In this case, while deciding the issue of rejection of plan by the Adjudicating Authority held that the Adjudicating Authority rightly observed that the resolution plan should be planned for insolvency resolution of the corporate debtor as a going concern and not for addition of value with intent to sell the corporate debtor. The purpose to take up the company with intent to sell the corporate debtor is against the basic object of the I&B Code. Further, the Hon'ble NCLAT noted that as more than 270 days have passed, the Adjudicating Authority having passed order of liquidation and directed that the liquidator to ensure that the company remains a going concern and certain other direction has been issued it is necessary that additional directions are required to be followed by the liquidator. The Hon'ble NCLAT proceeded to direct that in addition to directions of the Adjudicating Authority, the liquidator must also follow the decision and direction of NCLAT in *Y. Shivram Prasad vs. S. Dhanapal & Ors. Company Appeal (AT) (Insolvency) No. 224 of 2018.*

The aforesaid judgments of S. C. Sekaran and S. Dhanpal have been followed by the Hon'ble NCLAT and other NCLT's in various judgments which reinforces the evolving jurisprudence of revival of the company by way of scheme of arrangement under section 230 of the Companies Act, 2013 which are facing liquidation under the Code.

Conclusion

It is evident that the Courts have been very liberal in terms of sticking to the basic objective of the legislation, i.e., resolution and maximisation of value of assets and the death of the company by liquidation must be the last resort. Till the very end, they are ready to look into the resolution scheme for the betterment of the company and in addition to the liquidator such scheme can also be filed by the stakeholders including promoters. However, there is a need of suitable amendments in the regulations made under the Code so that the entire process of scheme of arrangement can be streamlined and it remains in harmony with the provisions of the Code.

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Default by successful bidder post approval of plan by NCLT

Tejas Davda
Company Secretary

DEFAULT BY WINNING BIDDERS

Need for Insolvency and Bankruptcy Code ("Code")

How much so ever we think of Indian economy, taking its infant steps towards being a developed economy, we somehow ought to admit and sip in with a pinch of salt that India's banking industry is in the throes of crises, owing to the piling up of bad debts. Further, in ordinary parlance, it is hard for any business to act against its client(s), no matter what challenges it faces. The story has been no different for banks and the wider institutional lending platforms in India. Freeing up this money is crucial for the banking sector to go about its business. Many concerns have been existing and/or raised amongst international investors on the regulatory and country risks while providing financing to and/or investing in India. The Code has reinvigorated the stressed asset space with both strategic as well as financial investors being bullish about the prospects of investment.

Objective of the Code

The enactment of the Code was aimed at addressing the problems of sick units in a time-bound manner by reorganising and achieving a resolution. The spirit of the law is to keep the entity a 'going concern'. The best part is the company will continue its operations.

For the bleeding companies and non-performing assets, the Code is a way out of the mess looming large over them due to the piled-up debt and the banking sector being saddled with bad books.

Pillars of Code - Equality, transparency, resolution and pace

Code is modelled towards maximisation of value of assets, striking a balance between liquidation and reorganisation, ensuring equitable treatment of similarly situated creditors, provision of timely, efficient and impartial resolution and ensuring a transparent and predictable insolvency law with incentives to gather and dispense information. The judicial orders that are transparently available in the public domain provide the perfect opportunity to analyse the performance of the NCLT as an institution.

Journey so far

There have been four deaths for every revival case under the Code proceedings, and significantly for those four, which have headed for liquidation, the process continues without much progress and hardly any takers.

Further, of the 1,858 cases taken up for resolution and finding a suitor for a revival plan, more than 1,000 are still under various stages of proceedings at the National Company Law Tribunal (NCLT).

As on March 31, 2019, of the total 1,858 cases admitted under insolvency proceedings, 94 achieved resolution, 243 were settled by mutual consent or appeals, and 378 companies/cases were taken up for liquidation. And, the rest are still undergoing the corporate insolvency resolution process (CIRP).

Even as the time taken for resolution under the Insolvency and Bankruptcy Code (IBC) continues to exceed the outer limit prescribed under the law, the process is yielding better outcomes in a shorter time frame as compared to the erstwhile regime. In FY19, financial institutions recovered close to ₹ 70,000 crore through resolution under the IBC, This works out to a recovery rate of 43 per cent. In comparison, recoveries under the preceding regime through various channels – debt recovery tribunals, securitisation and reconstruction of financial assets, and enforcement of the securities interest act (SARFAESI) and Lok Adalats – stood at ₹ 35,000 crore in FY18.

In the months after the IBC kicked in, operational creditors had taken the lead in initiating the corporate insolvency resolution process (CIRPs) against errant debtors. But thereafter, financial institutions stepped up. In fact, in the quarter ended March 2019, the number of CIRPs initiated by financial creditors exceeded those initiated by operational creditors.

Process of Resolution

The insolvency resolution process (IRP) is one under the Insolvency and Bankruptcy Code, 2016, where the National Company Law Tribunal (NCLT) initiates a corporate insolvency resolution process (CIRP) when a company defaults on making payment to creditors. A financial creditor, operational creditor or corporate itself can file an application before NCLT for initiating IRP when default has occurred. In case of housing project, after amendment in the code, a homebuyer can also approach NCLT for initiating IRP if a developer fails to provide possession of the house or refund the money.

Under IRP, an interim resolution professional is appointed with the power to take charge of the company which has defaulted. The professional's task is to take necessary steps to revive the company. Appointed professional also has the power to raise fresh funds to continue operations.

The IRP is granted 180 days to find a resolution, which can be extended by 90 days. If the IRP fails to find a resolution by then, the company is liquidated to pay the creditors.

What is Resolution Plan

A resolution plan is a proposal that aims to provide a resolution to the problem of the corporate debtor's insolvency and its consequent inability to pay off debts. It needs to be approved by 75% of the COC and comply with some mandatory requirements prescribed in the Code. Once approved, the Resolution Professional (**"RP"**) will send the plan to the **NCLT** after certifying that the plan meets those requirements. If the NCLT is also satisfied that the plan meets the requirements, it will pass an order approving the plan. where the NCLT approves the resolution plan, it becomes final and binding upon the corporate debtor and other stakeholders under the resolution plan. Other than the mandatory requirements, the Code does not restrict the form and manner of a resolution plan. A plan could therefore, involve the purchase of the equity or assets of the corporate debtor, the infusion of additional debt, the de-merger of debtor's businesses, financial "haircuts" taken by creditors, or the extinguishment of some liabilities. Needless to say, since the plan must be first approved by the COC – a body that comprises all the financial creditors of the corporate debtor, the proposals regarding debts owed to financial creditors will be an important consideration in whether it is approved.

Who can propose a Resolution Plan

Since the Code emphasises maximising the number of resolution solutions, its definition of a "resolution applicant" is simply, "any person who submits a resolution plan to the resolution professional". While the expectation from this wide definition is that the market at large will be the primary source of resolution plans, it is also open to creditors, and until very recently, the erstwhile promoters of the corporate debtor, to propose resolution plans. The RP moreover, does not have any discretion regarding which plans to present to the CoC – he or she is statutorily bound to present all plans that meet the mandatory requirements. In practice, the CoC typically authorises the RP to prescribe eligibility and evaluation criteria for resolution applicants so as to ensure that only serious applicants submit plans.

Who can be affected by a Resolution Plan

Section 31(2) of the Code makes the resolution plan, once approved by the NCLT, binding on "the corporate debtor and its employees, members, creditors, guarantors and other stakeholders involved in the resolution plan". The term "other stakeholders" here, is unclear.

Successful Bidder, Failed Resolution

While the Code has proven to be (or made to be) contentious in what seems to be almost every aspect of its substance and procedure, a new facet has been added to the realm of concerns under the new insolvency regime. However, concerned over several instances of successful bidders under the insolvency resolution process for stressed companies failing to make the promised payments on time – the most prominent one being that of UK-based Liberty House (Liberty) in the Amtek Auto^ and Adhunik Metaliks case have opened up the proverbial Pandora's box of shortcomings and indecisions under the Code.

Liberty's Games: London-based Liberty House, headed by Sanjeev Gupta, was one of the big movers & shakers in the bankruptcy business three years ago. It was always rumoured in business circles that Liberty House had no plan to hold on to the companies after getting them cheap. Now, it has messed up the resolution process and obstructed serious bidders in its three winning bids for ABG Shipyard, Amtek Auto and Adhunik Metaliks.

ABG Shipyard: On 25th April, NCLT (National Company Law Tribunal) ordered the liquidation of ABG Shipyard after Liberty House failed to pay up the small upfront fee on its ₹ 5,200-crore bid. ABG Shipyard owes a massive ₹ 18,245 crore to a consortium of 22 lenders, led by ICICI Bank. They would be lucky to recover even ₹ 2,200 crore, on liquidation.

Amtek Auto: Liberty House won Amtek Auto with an offer of ₹ 4,400 crore in July 2018. After it failed to pay up, NCLT's Chandigarh bench recommended prosecution and allowed it to withdraw the bid after imposing a cost on it. On 4th May, IBBI filed a criminal complaint against Liberty House under Section 74(3) of Code which, provides for prosecution and punishment including a jail term of up to five years and a penalty of up to ₹ 1crore. Liberty House tried to justify such default came up with frivolous arguments. NCLT declined to entertain the application by the Liberty House contending that the difference between the book value and the liquidation value of Amtek Auto Ltd. is immoderate and the issue came in light for them only after the resolution was passed.

(^At least seven companies under the Insolvency and Bankruptcy Code (IBC) are staring at a situation where preferred bidders have raised issues, or have delayed, or just expressed a desire to walk away from implementing a resolution plan. Three companies – Castex Technologies, ARGL, Metalyst Forgings – are subsidiaries of Amtek Auto.)

Adhunik Metaliks Ltd.: Here, too, Liberty has missed multiple deadlines to pay up the ₹ 410 crore as an upfront cash payment. Liberty House has certainly derailed a proper resolution because Adhunik had other serious bidders wanting to acquire the company.

Legal Recourse

Where the successful bidder fails to honour its obligations under the approved resolution plan, the following recourse is available to the CoC:

Punishment for Contravention of the Resolution Plan

Section 74 of the Code says 'any person' bound by an approved resolution plan "knowingly and wilfully contravenes any of the terms of (such plan)… shall be punishable with imprisonment of not less than one year, but may extend to five years, or with fine which shall not be less than one lakh rupees, but may extend to one crore rupees, or with both".

There's merit in government setting up strong deterrents to ensure that the resolution applicants do not default on their proposed plans. The deterrents could range from a penalty amount (linked to the realisation promised to the creditors under the resolution plan) to debarring the resolution applicant from participating in any future CIRPs. Stringent deterrents will reduce instances of completed CIRPs being brought back to the NCLT benches.

Amendments to the Approved Resolution Plan

Once a resolution plan is approved by the adjudicatory authority, it becomes binding upon all concerned parties. For this reason and in absence of any provision permitting deviation from the terms of the resolution plan, amendments to the resolution plan are not permitted under the Code and terms approved by the NCLT would prevail.

Considering another Bidder?

Owing to the binding nature of the approved resolution plan and in the absence of any provision under the Code for switching resolution applicants, following the approval of the resolution by the successful bidder, it must be concluded that the same is impermissible under the Code. The same view was affirmed by the Kolkata Bench of the NCLT on a petition brought by the CoC of Adhunik Metaliks to be able to consider the bid of another bidder.

Liquidation Route?

From the previous analysis it may seem that liquidation of the company would be the only real option available; however, on a bare perusal of the Code, another instance of the lacuna under the Code with regard to the enforcement or treatment of the failure is manifest. Under section 33 of the Code, various grounds for the liquidation of the corporate debtor are stipulated. Moreover, under section 33(3) of the Code, which talks of liquidation in the face of a failure of implementation of the resolution plan, the same is limited to instances where it is the corporate debtor which has violated the terms of the resolution plan. Furthermore, this option is only available to persons other than the corporate debtor whose interest is prejudicially affected by the contravention. Herein, the intent behind the provision is manifest as being a recourse against the malfeasance of the corporate debtor and the recourse is predicated upon the same under section 33(4) of the Code. In the present circumstances, the position is such that liquidation itself is not an option.

Changes to the IBBI Regulations

In a reactionary measure to the above-mentioned lacuna in the Indian insolvency regime, the Insolvency and Bankruptcy Board of India (IBBI) has brought about certain changes under the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (the CIRP Regulations) months after Liberty House reneged on its promises under the respective approved resolution plans. These changes are as follows:

1. Firstly, Regulation 36B(4A) of the CIRP Regulations stipulates that the resolution applicant must provide a "performance security" as part of a resolution plan, where such a plan is approved. The same may be forfeited where the resolution applicant fails in the implementation of or contributes to the failure of that plan in accordance with the terms and

implementation schedule of such a plan. The "performance security" would be a security of such nature, value, duration and source, as may be specified in the request for resolution plans with the approval of the committee, having regard to the nature of resolution plan and business of the corporate debtor. Furthermore, a performance security may be specified in absolute terms or in relation to one or more variables such as the term of the resolution plan, the amount payable to creditors under the resolution plan, and the like.

2. Secondly, a resolution plan must include a statement giving details if the resolution applicant or any of its related parties has failed to implement or contributed to the failure of implementation of any other resolution plan approved by the adjudicating authority at any time in the past [Regulation 38(1B)].

While the abovementioned provisions do bring some respite, the resolution process is still left heavily exposed to the uncertainty of processes and the repercussions of failure when it comes to the violation of the approved resolution plan by the resolution applicant. Beyond these provisions, it is incredibly important to vest the NCLT and the National Company Law Appellate Tribunal (NCLAT) with the power to ensure the successful execution of the resolution plan. The reason for the same is that the public knowledge of the violation of the resolution plan deals an overwhelming blow to the market position of the corporate debtor, from which it is rarely possible to recover for an already insolvent and encumbered firm.

Learning Experience

The ongoing uncertainty in the Amtek Auto insolvency case after the 'successful' bidder Liberty House failed to pay creditors is a 'learning' experience for the entire insolvency regime. While this means start of the insolvency process from scratch, the case should force stakeholders to revamp the entire process and select a resolution plan more robustly to ensure that future bidders are fully committed. This is equally true for bidders - Liberty House, for instance, has been saying it was misled into buying Amtek Auto - who need a way to check the assets of companies they are trying to buy.

Conclusion

There has been a marked improvement in the recovery process which is already leading to billions of dollars being invested in the country due to the protection of creditor rights. Compared to other markets, the pace at which we have achieved this is also noteworthy.

It is imperative that we have more examples of efficient resolution (which includes successful implementation of the resolution plans) such as the resolution of Bhushan Steel by Tata Steel, since the time value of money is an important consideration to ensure the efficacy of the Code framework.

The present situation has unearthed a far-reaching lacuna under the Code which strikes at the very foundational objects of the Code which are timely resolution and the preservation of maximum economic value during insolvency. While the insolvent company is already suffering under a debt-laden position, it is the resolution applicant that voluntarily takes up the task of resolving such insolvency. However, it becomes a losing fight for the corporate debtor (along with its members and employees), its creditors and other relevant parties where the successful bidder itself fails to honour its obligations under the Code. Stringent and express provisions are the only real means by which this lacuna can be corrected, lest it rock the very foundation of the Code and its ambitious objects.

Role, Responsibilities, Powers and Risks of working as an IP


CA Pravin R. Navandar & CA Udayraj Patwardhan

Introduction

The Insolvency and Bankruptcy Code, 2016 ('the Code') is a reformative law which has substantially changed the scenario of the procedural law associated with insolvency and bankruptcy in India. Since its inception in the year 2016, the law has witnessed various amendments, in light of remarkable judicial precedents and multiple practical issues of material legal significance (presently, after NCLAT order dated 4th July 2019, in the case of Essar Steel) few more amendments to the Code are in process). Amongst the various designated agencies under the Code which are crucial for smooth functioning of the process of law, one of the agencies whose role has been significantly highlighted in the past three years of journey, is the Insolvency Professional ('IP'). IP is someone who is the hub to whom all the other spokes – agencies and stakeholders are attached and therefore acts as one of the institutional pillars under the Code.

Statutorily, an IP is a person registered as such under the provisions of section 206 of the Code, with an Insolvency Professional Agency as its member and registered with the Insolvency and Bankruptcy Board of India ('IBBI') under section 207. An IP can act in multifarious capacities; IP can act as an Interim Resolution Professional or a Resolution Professional during the Corporate Insolvency Resolution Process ('CIRP') or as a Liquidator in case of Liquidation/Voluntary Liquidation process. IP also acts as a bankruptcy trustee for individual and partnership firms. IP is authorized to represent Financial Creditors in a meeting of Committee of Creditors on their behalf.

Additionally, an IP should possess excellent skills and competence to ensure maximum diligence and care in handling the process which involves active involvement, analytical and judgment skills. His approach must be aligned with the intent of law. Due to the ineffectiveness of erstwhile insolvency laws, processes and failure of existing institutions/mechanisms such as DRT, SARFAESI, SICA, etc., there has been a need for turnaround specialists and industry experts to run and manage resolution process and facilitate revival and maximization of value to stakeholders. This need seems to be fulfilled by IPs.

In light of the importance of the role played by an IP, it is pertinent to understand the role and responsibilities, powers held and risks undertaken by an IP as per the Insolvency and Bankruptcy Code, 2016. This article discusses each of these aspects in brief and other associated issues. The procedural responsibilities under the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 are not covered under this article.

Role, responsibilities and duties

1. ***Preserve the value of properties*** – An insolvent corporate debtor, for which corporate insolvency resolution process has commenced, is one step away from the pitfall of Liquidation. Hence, it is the duty of IP as an RP to make the efforts to preserve the value of properties and endeavour that these properties fetch the maximum value possible. RP should ensure that all the personnel who are responsible for security of the properties are retained and paid on time. Any incidence which raises any alarms must be addressed properly.

2. ***Management of affairs of corporate debtor as a going concern*** – Maintenance of the going concern aspect of the Corporate Debtor is essentially the most important aspect of the resolution process. RP must ensure smooth functioning of operations of the Corporate Debtor. While ensuring the same, RP should seek to either continue the operations in case of existing operations, or restart stalled operations, wherever possible.

3. ***Collation and verification of claims*** – It is the IRP's responsibility to take all the received claims on record and verify the same on the basis of books and records of the Corporate Debtor. Post verification, RP is required to collect and verify all the claims received by him. NCLAT order in the case of Essar Steel dated 4th July 2019[1] held that RP has no jurisdiction to admit or reject a claim. This is within the powers of NCLT, in case of any grievance thereof. Based on the verification, the RP prepares the list of creditors and also updates the same.

4. ***Constitution of CoC*** – IRP is required to constitute a Committee of Creditors ('CoC') comprising of all financial creditors, with few exceptional instances as provided under the Code. The members of CoC have voting rights in proportion to their claim amount *vis-à-vis* the amount of total debt.

5. ***Organising meetings and maintaining records*** – All the meetings of CoC are organized by RP and all the proceedings of such meetings must be recorded and circulated to the members. He is required to circulate the minutes of the meeting within 48 hours. IP shall also provide the facility of e-voting and participation in meeting through audio-visual means, etc.

6. ***Appointment of required consultants or professional*** – For adequate performance of his duties as RP or Liquidator, IP can appoint various professionals to assist him, as and wherever required. Further, RP shall appoint two registered valuers to determine the fair value and the liquidation value of the corporate debtor in accordance with Regulation 35 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 ('CIRP Regulations'). The valuation report is to be kept confidential.

7. ***Custody of the assets*** – Insolvency Professional, as an RP/Liquidator must take the custody of all the assets and documents owned and belonging to the Corporate Debtor. There may be instances where the asset is not in possession of the Corporate Debtor, however, the ownership rights are vested in it. Such assets shall also be taken into custody.

1. To be reconsidered in the hearing scheduled on 24th July 2019 before Hon'ble Supreme Court.

In his endeavour to take the custody of assets, the Insolvency Professional may experience certain difficulties, such as non-cooperation from the Corporate Debtor. Excessive resistance may hamper the custody transfer. In case of *Central Bank of India vs. M/s. Ashok Magnetics Ltd.*[2], NCLT directed the Superintendent of Police to give proper police assistance and personal security to the IRP so that he can take charge of the assets of the Corporate Debtor and perform the functions as per the provisions of the Code. Similar assistance for the purpose of factory visit was granted to RP in the case of *Punjab National Bank vs. Divyajyoti Sponge Iron Pvt. Ltd.*[3]

8. ***Collect information and updates*** – IRP/RP must collect all the relevant information relating to the assets, liabilities, finances and business operations of the Corporate Debtor. He must keep himself updated and monitor such assets and business operations.

9. ***Preparation and submission of various documents*** – All the documents that are required to be submitted to CoC, Adjudicating Authority and IBBI, are required to be prepared and thoroughly vetted by RP/Liquidator. One of the key documents in the process is the Information Memorandum ('IM') which is required to be submitted to members of CoC and also to the prospective resolution applicants. IM shall contain the details of assets and liabilities, financial statements, list of creditors, details of debt, details of shareholders, etc. The contents of IM are also required to be regularly updated. The information sought by Resolution Applicant/s is also required to be provided by RP. Normally, RP avails the service of Data Room and gives access of the same to all Resolution Applicants.

10. ***Duties w.r.t. Resolution Plan(s)*** – RP is mandated to invite expressions of interest from prospective resolution applicants to submit resolution plans and shall share the IM, evaluation matrix and request for resolution plans to the prospective applicants. On receipt of resolution plans, RP must examine each one of these plans and present before CoC such plan(s) which complies with the requisite conditions. Once approved, he must submit the plan to NCLT for its final approval.

11. ***Duties w.r.t. avoidance application and forensic audit*** – RP shall file application within a period of 75 days for avoidance of transactions in accordance with Chapter III of the Code, as and where required in the following instances:

a. Preferential transactions u/s. 43

b. Undervalued transactions u/s. 45

c. Avoidable transactions u/s. 46

d. Undervalued transactions u/s. 47

e. Transactions defrauding creditors u/s. 49, and

f. Extortionate credit transactions u/s. 50

12. ***Liaising with various stakeholders*** – During the entire process of CIRP and Liquidation, the IP acts as the central agency to ensure seamless communication.

2. CP/551 (1B)/CB/2017
3. CA (IB) No. 570/KB/2017

Role of IP vs. role of the Board of Directors

On appointment of IRP, the powers of the Board of Directors are suspended, however, the onus and responsibilities of the Directors is not affected. In fact, during resolution, the whole intent is to resolve the Company. In order to do so, the RP has to ensure that the identity of the Company as a going concern is intact. To ensure this, the regular transactions or actions or any duty required to be performed by the directors, to ensure adequate compliance of applicable laws, must continue without any exception.

Rights and powers of IP

1. ***Transfer of Board powers to IP*** – On appointment of IRP/RP, the Board of Directors of the Corporate Debtor gets suspended and all the powers which would be exercised by the Board, are transferred to IP for continual decision making. All the staff members and existing management are required to report to IP.

2. ***Access to all the records of Corporate Debtor*** – An IP has access to all the records and information about the Corporate Debtor, including electronic records from Information Utility.

3. ***Operation of bank accounts*** – All the bank accounts of the Corporate Debtor are operated by the RP/Liquidator. He shall have the sole authority to instruct any transfer from/to these bank accounts or any closure, thereof.

4. ***Act and execute on behalf of Corporate Debtor*** – All the documents, contracts and transactions are executed by the RP or the Liquidator, on behalf of the Corporate Debtor.

5. ***Authority to appoint professionals*** – RP appoints such professionals, as may be required to ensure operations of the business on a going concern basis.

6. ***Raise interim finance*** – RP has the authority to raise interim finance provided that no security interest shall be created over any encumbered property of the corporate debtor without the prior consent of the creditors whose debt is secured over such encumbered property.

7. ***Powers to be exercised only after approval of CoC*** – In addition to above, there are certain powers that the RP can exercise only after obtaining prior approval of CoC, (See section 28 of the Code) such as:

    a. Raise interim finance in excess of amount decided by CoC

    b. Create security interest on Corporate Debtor's assets

    c. Change in capital structure of Corporate Debtor, etc.

Risks of working as an IP

1. ***Unfamiliarity with the business of Corporate Debtor*** – An Insolvency Professional who is otherwise qualified and competent to perform his duties effectively as an RP/Liquidator, may lack adequate experience in the industry or business in which the Corporate Debtor operates. This may hamper his ability to perform in his best capacity to revive the business operations.

2. ***Management incompetency*** – Without any exception to the knowledge and expertise of the IP, he might not possess the relevant management skills to run the business operations on a day-to-day basis and take key decisions in an effective fashion.

3. ***Non-cooperation from employees or management*** – An RP needs active cooperation from the employees, management, ex-directors of the Corporate Debtor to effectively discharge his duties. Non-cooperation from such individuals would restrict the performance and completion of process on time.

4. ***Unfamiliarity with the specific laws applicable on Corporate Debtor*** – Each Corporate Debtor is governed by specific laws, other than common laws, which are specific to the industry in which the Corporate Debtor operates. The IP is not necessarily accustomed or aware of all such applicable laws. This may result in unnecessary delays.

5. ***Litigation risks*** – Since RP operates individually, to monitor and operate the business and also the resolution process, he is vulnerable to litigation risks. It is practically not possible to act in the best interest of all the stakeholders and thus, in the process of resolving the Corporate Debtor, he may end up facing law suits filed by dissented creditors or aggrieved stakeholders.

   However, protection is granted to IRP/RP, who act in good faith under section 233 of the Code. In one such interesting case of *M/s Alchemist Asset Reconstruction Co. Ltd. vs. M/s. Hotel Gaudavan Pvt. Ltd.*[4], NLCT observed that any such complaint can only be filed by IBBI. A complaint filed by any other person shall not be maintainable under section 236 of the Code.

6. ***Health risks*** – In continuation to the above point, excessive involvement may pose threat to the mental and physical health of the Insolvency Professional to a certain degree.

7. ***Professional risks*** – Performance of duties as RP/Liquidator requires substantial devotion of time and energy into the relevant matters. This may result in lesser involvement of the IP in his own professional practice that he could be engaged in otherwise, in other areas of his expertise.

8. ***Financial risk*** – The revenue generated from services provided by RP/Liquidation are highly subjective and depends upon the demand and available cases. There is an inherent financial risks, *vis-à-vis* fluctuations in the matters and demand.

9. ***Other risks and protection*** – IP may be exposed to other types of risks while fulfilling his duties as an RP. In the matter of *Asset Reconstruction Company (India) Ltd. vs. Shivam Water Treaters Pvt. Ltd. MA 876-2019 in CP (IB) 1882(MB)-2018;* NCLT, Mumbai, Order dated 15th April, 2019, the adjudicating authority directed the ex-directors of the Corporate Debtor to hand over all the documents pertaining to the Corporate Debtor, to allow the RP to take possession and control of the registered office, corporate office and factory premises within a limited period of 3 days from this order.

Conclusion

The Code is still fresh and in its implementation stage. There is abundant potential for evolvement of law in light of judicial pronouncements and amendments. An Insolvency Professional is the backbone of the entire process of resolution. Therefore, he must be an individual with independent judgment and highest ethical standards as every decision he takes, may substantially impact the interest of the stakeholders involved. In short, irrespective of all other important factors, the capability of the IP can decide the success or failure of the resolution process of a Corporate Debtor.

4. CP/CA. No. (IB)-23(PB)/2017

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Amendments to The Insolvency and Bankruptcy Code, 2016 ...What it Means?

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Introduction

The Insolvency and Bankruptcy Code, 2016 (**IBC**) was enacted with the objective to consolidate and amend laws relating to insolvency process in a time bound manner for maximization of value of assets of corporate persons, partnership firms and individuals, to promote entrepreneurship, and develop credit markets, amongst others. The IBC is one of the most lauded legislative reforms in recent times which has contributed to India's rise in the World Bank's 'Ease of Doing Business' ranking and received positive attention from foreign investors. However, since the implementation of the IBC in December 2016 there have been several amendments to it and the regulations thereunder to plug in loopholes in the implementation of the provisions of IBC and to provide solutions to practical unforeseen challenges that have given rise to a host of litigations.

The first amendment to the IBC brought section 29A and introduced a major change relating to ineligibility of resolution applicant, *vide* the Insolvency and Bankruptcy Code (Amendment) Ordinance which was issued on 23rd November 2017 and later converted to the Insolvency and Bankruptcy Code (Amendment) Act 2018 on 18th January 2018. The second amendment was issued in the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 on 6th June 2018, which was later converted into the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 in August 2018 (*effective on the date of Ordinance*) and introduced the following amendments, amongst others: (a) home buyers were recognised as financial creditors and could initiate corporate insolvency process against the builders [*Explanation to section 5(8)(f)*], (b) decision of committee of creditors (**CoC**) allowed with 51% voting and 66% for important decisions as opposed to 75% voting required in all cases earlier [*Section 21(8) & Section 22(2)*], (c) withdrawal of application after admission, if 90% of CoC approves by voting [*Section 12A*], (d) trustee or agent of financial creditors can be appointed as authorized representative on CoC where financial debt is in form of securities of deposits [*Section 21 6A(a)*], (e) prior approval of Competition Commission of India is required prior to approval of the resolution plan, if required in the plan [*Proviso to Section 31(4)*], (f) promoters and guarantors of MSME can apply as resolution applicant even if they are in default of corporate debtors [*Section 29A(h)*], (g) moratorium granted to corporate debtor will not apply to enforcement actions against surety (guarantors) of corporate debtors [*Section 14(3)*], and (h) separate approval of shareholders is not required once resolution plan is approved [*Explanation to Section 30(f)*].

The Supreme Court in several of its landmark decisions has given importance to the spirit of the IBC rather than the procedural requirements stipulated in the IBC. However, several decisions of the tribunals in the recent past has created pessimism in the investment market and an increased perception that the objectives of the IBC are at risk of being derailed. Therefore, the recent news on Union Cabinet approving the proposal to introduce the Insolvency and Bankruptcy Code (Amendment) Bill, 2019 (**2019 Bill**) is a welcome change and gives hope that the legislative purpose for which the IBC was introduced will continue to be pursued and clarified and, in doing so, assist the judiciary in interpreting the IBC in a manner consistent with the legislative intent. This article analyses the salient features of the proposed amendments in the 2019 Bill, relevant judicial precedents that triggered the amendments and suggests a way forward so that the objective of IBC may be adhered to in letter as well as in the true spirit of the law.

As per the press release dated 17th July 2019 issued by the Ministry of Corporate Affairs, the 2019 Bill aims to fill in the critical gaps in the corporate insolvency resolution framework while simultaneously maximizing the value from the corporate insolvency resolution process (**CIRP**). The 2019 Bill will need to be passed in both the Houses of Parliament and get the President's nod before it becomes a binding law. The key provisions proposed in the 2019 Bill are as follows:

a) ***Clarity on the inclusion of alternative restructuring schemes such as mergers, demergers and amalgamations as part of the resolution plan***

Presently, the IBC does not provide any provisions on the inclusion of alternative restructuring schemes as part of the resolution plan. However, in the absence of specific regulations, the resolution applicants have been framing resolution plans to include alternative restructuring schemes such as mergers, demergers and amalgamations as part of the resolution plan. The implementation of such plans are yet to be tested. The regulations would need to align such proposal with other relevant laws in force. For. e.g. if a scheme of merger or demerger under the Companies Act, 2013 is proposed, then the relevant provisions in the IBC will need to be aligned with respect to timeline, payment of stamp duty on the order of the scheme and tax considerations under the respective laws.

b) ***Time bound disposal at application stage and a proposal to extend the deadline for completing insolvency resolution from 270 days to 330 days, including the time spent in litigation or judicial process after the plan is admitted***

The IBC prescribes a time period within which the CIRP is required to be completed. Section 12 of the IBC states that CIRP should be completed within 180 days from the date of admission of the application to initiate the CIRP and grants additional 90 days period, if the adjudicating authority is of the view that the CIRP cannot be completed within 180 days. The judiciary has been allowing extensions of this statutory time limits by excluding time spent in litigation. However, this has resulted in inordinate delays that risk the intent of the legislation to ensure time-bound resolution being overridden in practice. As per the data published by the Insolvency and Bankruptcy Board of India (**IBBI**), since commencement of the IBC on 01 December 2017, about 1858 corporate debtors have been admitted into CIRP till end of March, 2019, of which, 152 have been closed on appeal or review or settled, 91 have been withdrawn; 378 have ended in liquidation and only 94 have ended in approval of resolution plans. As per the said data, out of the 94 cases in which resolution plans have been approved as of March 2019, around 72 have exceeded 270 days, 22 have exceeded 300 days, nine have exceeded 400 days, four have exceeded 500 days and three have exceeded 600 days. The amendment of extending to 330 days (including the time spent in judicial process) is a positive step as the mandatory timeline will discourage resolution applicants from filing frivolous cases and stalling the CIRP, but to comply with this timeline, the other timelines under the IBC with respect to admission or rejection of application of initiation of CIRP by the National Company Law Tribunal (**NCLT**) and the last date of filing of claim by creditors will have to be strictly adhered to and made mandatory.

c) ***Votes of all financial creditors covered under Section 21(6A) shall be cast in accordance with the decision approved by the highest voting share (more than 50%) of financial creditors on present and voting basis***

The last amendment to the IBC introduced that trustee or agent of financial creditors can be appointed as authorized representative on CoC where financial debt is in form of securities of deposits. This instant amendment clarifies that the manner in which such trustees under Section 21 (6A) shall vote in accordance with the highest voting share of financial creditors on a present and voting basis. This issue was also deliberated in *IDBI Bank Ltd. vs. Jaypee Infra Ltd.* (CP No. (IB) 77/ALD/2017) wherein the main question was whether the various threshold voting share fixed for the decision of the CoC under various sections of the IBC needs to be followed literally or whether they are only directory, and if so, what procedure has to be followed in determining the voting percentage among the CoC to pass a particular resolution. The NCLT Allahabad Bench held that *"Under Section 21(2) of the IBC, the CoC shall comprise entirely of financial creditors and they have to be construed as one, it cannot be segmented class wise for the computation of voting share. For the computation of voting share required to be achieved, class wise voting of financial creditors and to treat the majority vote of that particular class by adding the voting share of those financial creditors who had abstained as the will and vote of the entire class in the CoC cannot be accepted".*

d) ***A specific provision with regard to equating the distribution of amounts under a resolution plan in accordance with section 53 of the Code or in case of liquidation, maintaining the hierarchy of lenders. The change will be retrospective, making it applicable for ongoing cases***

The amendment has been brought in with retrospective effect to salvage the situation created by the recent National Company Law Appellate Tribunal (**NCLAT**) decision in *Standard Chartered Bank vs. Satish Kumar Gupta, R.P. of Essar Steel Ltd. & Ors* (Company Appeal (AT) (Ins.) No. 242 of 2019) on 4th July, 2019 (**Essar Steel Case**) and gives hope to the investors by reiterating the hierarchy of creditors in a liquidation process under Section 53 of the IBC which gives priority to secured creditors above the unsecured and operational creditors.

The NCLAT in the Essar Steel Case while deliberating on the issue of distribution of debts to the 'Financial Creditors' and the 'Operational Creditors' during the 'Corporate Insolvency Resolution Process' observed that *"A 'Resolution Plan' shows upfront payment in favour of the Creditors including the 'Financial Creditors', 'Operational Creditors' and the other Creditors. It is not a* *distribution of assets from the proceeds of sale of liquidation of the 'Corporate Debtor' and, therefore, the 'Resolution Applicant' cannot take advantage of Section 53 for the purpose of determination of the manner in which distribution of the proposed upfront amount is to be made in favour of one or other stakeholders namely– the 'Financial Creditor', 'Operational Creditor' and other creditors".*

The Appellate Tribunal held that that the distribution of debts to the 'Financial Creditors' and the 'Operational Creditors' during the 'Corporate Insolvency Resolution Process' cannot be equated with distribution of debts to all stakeholders after the liquidation and held "Section 53 cannot be made applicable for distribution of amount amongst the stakeholders, as proposed by the 'Resolution Applicant' in its 'Resolution Plan'." NCLAT further held that "the 'Financial Creditors' cannot be discriminated on the ground of 'Secured' or 'Unsecured Financial Creditors' for the purpose of distribution of proposed amount amongst stakeholders in the 'Resolution Plan' by the 'Resolution Applicant'." This decision has caused major unrest to the distressed assets market in India. The consortium of lenders led by State Bank of India challenged the NCLAT order before the Supreme Court on 16th July 2019. The Supreme Court on 22nd July 2019 has said that the order is not to be given effect as of now and hopefully this amendment will be codified soon and provide the necessary guidance as to legislative intent to the Supreme Court.

e) Inclusion of commercial consideration in the manner of distribution proposed in resolution plan, within the powers of the CoC

This amendment is critical as it clarifies that judicial authorities cannot tweak or suggest changes in the commercial aspect of distribution of proposed in the resolution plan. The proposal empowers the CoC to decide on how the claims will be distributed based on commercial consideration determined by experts. This is in line with the Supreme Court decision in *K. Sashidhar vs. Indian Overseas Bank & Ors.* [Civil Appeal No. 10673/2018] wherein it observed: *(a) The word "may" in section 30(4) is ascribable to discretion of CoC to approve or reject resolution plan. Resolution Professional (**RP**) is not required to express opinion on matters within the domain of financial creditors (FCs), to approve or reject resolution plan. IBBI cannot, under section 196, directly or indirectly regulate the manner of exercise of commercial wisdom by FCs during the voting on resolution plan. Appellate Authority (**AA**) has no jurisdiction to evaluate commercial decision of CoC much less to enquire into the justness of rejection of plan by dissenting FCs. (b) If resolution plan is approved by CoC, it is obligatory for RP to submit it to AA. If plan is rejected by not less than 25% of voting shares of FCs, RP is under no obligation to submit it under section 30(6) to AA. The legislative intent is to uphold the opinion of the minority dissenting FCs. On receipt of the plan, the AA is required to satisfy itself that the plan approved by CoC meets the requirements specified in section 30(2). Upon receipt of a "rejected" resolution plan, the AA is not expected to do anything more; but is obligated to initiate liquidation process under section 33(1).*

The recent *Essar Steel Case* also observed that *"The 'I&B Code' provides for 'Corporate Insolvency Resolution Process' for reorganisation of 'Corporate Debtors'. It separates commercial aspects from judicial aspects and empowers and facilitates the 'Committee of Creditors' to take commercial decisions in a 'Corporate Insolvency Resolution Process'. The commercial decisions of the 'Committee of Creditors' are not ordinarily* *open to any analysis, evaluation or judicial review by the Adjudicating Authority or the Appellate Authority and hence not justiciable.*

f) Clarification that a plan will be binding on all stakeholders including the central and any state government or a local authority which has dues from a corporate debtor

This amendment is a most welcome clarification and reinforces the binding nature of the resolution plan making it binding on all stakeholders including the Central and any State Government or a local authority which has dues from a corporate debtor. In *Vijay Kumar Jain vs. Standard Chartered Bank & Ors.* (Civil Appeal No. 8430 of 2018), the court deliberated the above mentioned point and referred to Section 31(1) of the Code and affirmed the fact that *"The Adjudicating Authority under Section 31(1), if satisfied that the plan passes muster, shall then, by order, approve such plan, which shall be binding on all stakeholders involved in the resolution plan, including guarantors. Additionally, the Court also observed that under Regulation 38(1)(a) of the Insolvency Resolution Process for Corporate Persons, 2016, which states a resolution plan shall include a statement as to how it has dealt with the interest of all stakeholders."*

g) The CoC may take a decision to liquidate a corporate debtor at any time after the constitution of CoC and before preparation of information memorandum

This amendment provides that the CoC may take a decision to liquidate a corporate debtor at any time after the constitution of CoC and before preparation of information memorandum. The Supreme Court in *Arcelormittal India Private Limited vs. Satish Kumar Gupta & Ors.* (Civil Appeal Nos. 9402-9405 of 2018), while discussing the issue on ineligibility of resolution applicants to submit resolution plans after the introduction of Section 29A into the IBC made certain observations amongst others about the power of the Committee of Creditors and noted that *"the Committee of Creditors which will approve or disapprove a resolution plan, given the statutory parameters of Section 30."* In this case Supreme Court held that *"We make it clear that in the event that no plan is found worthy of acceptance by the requisite majority of the Committee of Creditors, the corporate debtor, i.e. ESIL, shall go into liquidation."*

Conclusion

The proposed amendments are encouraging and boosts confidence in the market when investors were starting to lose interest due to recent judicial developments. The time-bound reorganization and resolution for stressed assets being the most important focus of this amendment, it is crucial for the government and the judiciary to keep strengthening the infrastructure at the NCLT, by improving case management and establishing more NCLT benches so as to minimise the delay in the resolution process and timely disposal of cases and by training judges and providing continued training and support to insolvency professionals to enhance their competence and improve professionalism in the resolution process. The overall impact of IBC has been positive and has tremendously helped address the issue of mounting non-performing assets in the banking sector. However, as reiterated by Supreme Court in several decisions, the focus of IBC must be ensure revival and continuation of the corporate debtor rather than liquidation and IBC should not be used as mere recovery legislation of the creditors.

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Tax Issues under Insolvency & Bankruptcy Code, 2016



CA Amrish Shah, CA Rahul Vig & CA Neha Gupta

"One thing is clear: The Founding Fathers never intended a nation where citizens would pay nearly half of everything they earn to the government." – Ron Paul

For corporates undergoing insolvency resolution proceedings, tax liabilities can be more than what they could imagine to earn.

Background

The Insolvency and Bankruptcy Code, 2016 (IBC or the Code) has encompassed numerous legislative measures for sick and insolvent companies into one holistic law. IBC has transformed the relationship between a creditor and a debtor with the former no longer chasing the latter. The Indian insolvency regime focuses on the recovery of distressed firms with creditors being an incidental follow-up. The timeframe for resolution and the risk of losing investment significantly reduced after the launch of IBC on 1 December 2016. The Code aims to address the non-performing assets crisis and remove barriers in credit availability, which can help boost growth.

After the introduction of the Code, the Indian corporate sector witnessed numerous high-profile lenders, and in some cases trivial creditors, dragging debt-ridden companies to the Court and attempting their sale (in part or whole). Up to March 2019, about 14,000 applications were filed to initiate the Corporate Insolvency Resolution Process (CIRP) under IBC. Of which, only 1,858 cases were admitted for resolution by National Company Law Tribunals (NCLTs)[1]. The problems under CIRP range from non-cooperation on part of promoters, confusion over the provisions of the Code, extent of powers of resolution professionals and courts, and apprehensiveness about the tax burden (which can arise on the transfer or acquisition of a business or its assets). These problems can be corroborated by the fact that only 94 cases reached successful resolution until March 2019; 378 cases of liquidation[2] have been approved so far.

Since the launch of IBC, several laws have been amended to incorporate IBC provisions and achieve its objectives. Jurisprudence will emerge and eventually the insolvency resolution process will become more effective.

1. Chapter 3 of IBBI Economic Survey 2018-19, Volume II.
2. IBBI Quarterly newsletter January–March 2019.

Tax scenario

While the IBC and other allied laws have given a head start for the speedy resolution of insolvency cases, some of their tax implications for critical issues need deliberation.

Some complexities have been addressed by amending the Income-tax Act (the Act):

i. ***Section 79***: Lapse of brought forward losses on a change of shareholding beyond 49 per cent under section 79 would not arise where a change was due to an approved resolution plan.

ii. ***Section 80***: The Insolvency Resolution Professional shall be authorised to sign the Return of Income (ROI) for companies undergoing CIRP.

iii. ***Section 115JB***: For a company against which NCLT has admitted a CIRP application, the aggregate amount of brought forward loss and unabsorbed depreciation are allowed as deduction to compute book profits for minimum alternate tax (MAT).

iv. ***Section 178*** on liquidation of companies: IBC has been amended to overrule provisions of this section. Thus, for cases where IBC applies, liquidator is not required to part with assets to settle tax liability.

Although some relief has been provided, some significant issues are yet to be resolved. This article tries to address tax-related issues faced by companies undergoing CIRP.

Waiver of debt

The most talked about tax issue under the Code pertains to the potential tax liability arising for insolvent companies on waiver of debt balances. Section 41(1) of the Act taxes any gain arising on waiver of a trading liability. The Apex Court in the case of *CIT vs. Mahindra and Mahindra Limited*[3] held that if a loan was obtained and used to acquire a capital asset and no deduction was claimed for the loan in the previous years, the waiver of such a loan is akin to a capital receipt and should not be subject to tax as business income under section 41(1). In respect of section 41(1), this view is supported by several judicial precedents[4], including *Iskraemeco Regent Ltd. vs. CIT*[5]. In a recent judgment of Compaq Electric Ltd.[6], SC relied on the aforesaid ruling of *Mahindra and Mahindra Limited,* upholding the decision of Karnataka High Court that receipt on waiver of a loan obtained in the ordinary course of business to be a capital receipt in the hands of assessee. However, there is still ambiguity around taxability of waiver of a trading liability under the current ambit.

Whether such waiver can also be taxed under the gift tax provisions of section 56(2)(x), is a matter that needs to be resolved. In the aforementioned case of *Mahindra and Mahindra Limited*, the decision pronounced waiver of loan akin to a capital receipt. Tax authorities may contend that waiver has resulted in a monetary benefit and accordingly proceed to tax the entire remission or waiver as income from other sources, on the ground that the company has received money without consideration.

There have been contrary rulings on whether waiver of a loan taken to acquire a capital asset will have an impact on the asset's actual cost and the resultant depreciation claim. One view says that if a part of the cost is met at the time of acquisition, the fixed asset's actual cost requires adjustment. When the loan is waived off after

3. 93 taxmann.com 32 (2018).
4. *CIT v. Cochin Company Limited* (Kerala High Court) (1990) (184 ITR 230); *Steel Authority of India vs. CIT* (Delhi High Court) (2012) (20 taxmann.com 198)
5. 196 Taxman 103 (2011) (Madras High Court).
6. 101 taxmann.com 400 (2019).

acquisition, such waiver would not reduce actual cost as taking loan and purchasing an asset are two dissimilar transactions. Hence, once the asset is acquired and actual cost is determined, the actual cost cannot vary merely because the loan is waived off by the lender or financier. Another view says that if loan is taken to acquire an asset and waived off, it can be construed as cost met by the lender or financier. Hence, such a loan should be deducted from cost of assets.

In addition, waiver amount can have MAT implications, depending on the treatment prescribed under the applicable accounting standards. Under the erstwhile Sick Industrial Companies Act ('SICA') regime, a blanket exemption was provided from MAT to distressed companies. However, no such exemption has been provided under the Code.

According to the amended MAT provisions, aggregate of brought forward loss (excluding depreciation) and unabsorbed depreciation can be claimed as deduction from the book profits by a company undergoing the resolution process. Accordingly, the corporate debtor will have to determine the balance of accumulated losses and unabsorbed depreciation to off-set the waivers obtained. Further, the amended provision does not refer to 'books of account' as provided in the original provision and should be clarified.

According to the language of the amendment brought under MAT by Finance Act, 2018, the benefit is available to the company whose application is admitted before NCLT. While the starting year for availing the benefit is specified, no sunset clause is provided. Due to lack of clarity regarding the above mentioned provision, companies might try to take a prolonged benefit or be subject to an early withdrawal of the benefit. Thus, the issue is not free from litigation.

The resolution plan's purpose is to turn the stressed company around, and make it more productive and profitable. To serve this purpose, all stakeholders contribute by waiving some of their claims on the company. If such waivers were taxed, this would place a burden on the company and require it to use cash to pay taxes when there is no real income.

Conversion of debt instruments

As an alternative to direct foregoing of receivables, lenders may choose to convert debt into equity. According to section 56(2)(viib) of the Act, if the consideration received for shares issued at a premium by a closely held company to a resident, exceeds the fair market value determined per Rule 11UA[7] of the Income Tax Rules, 1962, the difference between such fair value and the consideration is treated as other income in the hands of the issuer company.

Although the applicability of anti-abuse provisions on converting debt instruments into equity is a challenge for the company, similar taxability may also be triggered on issuing shares at a value higher than the value determined per Rule 11UA at the time of infusion of funds by successful resolution applicants.

Loans can be converted into equity or infusion by new shareholders at a higher value to achieve the commercially desired stake, and ensure that adequate time and funds are committed to the company for its revival. To tax premium in such situations would defeat the purpose of creating value in the company.

Also, if the accounting treatment is followed for converting debt instruments into equity instruments, (as prescribed under Indian Accounting Standard 109 'Financial Instruments' - 'Derecognition of Financial liability'), the

7. For the purpose of this section, the value as per Rule 11UA is to be calculated basis the net worth of the companies or determined by a merchant banker as per the discounted free cash flow method.

difference between carrying amount of debt extinguished and the value of equity instruments issued is recognised in the profit or loss statement, which can lead to MAT implications.

Renewal of outstanding interests as debt or equity

The resolution plan under IBC may involve converting interest portion into loan or equity as a way of debt restructuring between lenders and borrowers.

Following the decision in the case of *Commissioner of Income-tax vs. Rathi Graphics Technologies Ltd.*[8], it has been a settled position that any conversion of interest into equity shares should be treated as extinguishment of interest liability to that extent. Explanation 3C to Section 43B does not apply in this case as it talks about converting interest into loan or borrowing.

According to section 43B of the Act, interest payable on any loan or borrowing or advance from any scheduled bank or a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank, public FIs, state financial corporation or a state industrial investment corporation is allowed as a deduction only when such interest is actually paid by taxpayers.

The explanations 3C and 3D to section 43B specifically exclude interest that has been converted into a loan or advance for the purpose of deduction under section 43B by treating it as deemed to have been actually not paid.

Converting interest into loan, in line with the NCLT-approved resolution plan under IBC, would tantamount to corporate debtor losing interest deduction – an additional financial burden.

TDS deduction under section 194A

Section 194A of the Act requires any person other than an individual or HUF who is liable to pay interest (other than interest on securities) to a resident, to withhold tax at the time of payment or credit, whichever is earlier. Non-compliance with section 194A results in 'assessee' being treated as 'assessee in default' and attracts penalty provisions. A company undergoing CIRP may recognise interest liability in the books without depositing TDS on interest liability recognised in its books of account. This would render it non-compliant, leading to levy of interest and penalties that disrupt the revival process rather than supporting it. It would be worthwhile to consider relaxing this requirement in IBC scenario.

Applicability of anti-abuse provisions on acquisition or sale of shares

Pursuant to the resolution process, existing promoters are hardly paid any money by resolution applicants to acquire shares or securities of the corporate debtor. Per section 56(2)(x) of the Act, where any person receives a 'property' (including shares or securities) at a value less than the fair market value determined per Rule 11UA, the difference between such fair value and the consideration is treated as other income for the recipient.

The resolution process's purpose is to encourage acquirers to take over debt-ridden companies and turn them around, thus saving jobs and infrastructure. Many times, the value of such companies has been eroded substantially, but there is still a case for continuing profitable operations if they are appropriately managed. Taxing the receipt of shares in the hands of acquirer would make the resolution process inefficient and result in lower payment to existing lenders.

8. 235 Taxman 550 (Delhi High Court)/[2015].

The resolution plan may require the acquirer to take over the corporate debtor's management, including ownership at a nominal consideration, in a way that interests of creditors and employees, etc., are protected.

The risk of applicability of the aforementioned deeming provision may also apply when a company under CIRP undertakes capital reduction to eliminate its promoter shareholding. However, whether a company's own shares can be treated as 'property', as referred to in Section 56(2)(x), is a matter of debate.

Per section 50CA of the Act, if the consideration received or accruing because of the transfer of shares of an unlisted company is less than the fair market value determined per the Rule 11UAA of the Income-tax Rules, such fair value should be treated as sales consideration for calculating capital gains.

As part of the resolution plan, NCLT may mandate the sale of shares. When shareholders are losing much of their share value, reckoning a higher consideration for the sale of shares to the acquirer is not equitable. This may also result in a situation where tax is more than the sale consideration shareholders received for shares.

Budget 2019 witnessed a proposal to empower the board to prescribe transactions undertaken by certain classes of persons to which the provisions of section 56(2)(x) and 50CA shall not be applicable. It would be worthwhile if the transactions under IBC are notified in the list of exemptions in the near future.

Capital gains on transfer of a business unit or capital assets

Under CIRP regulations, the resolution professional assumes power to sell unencumbered assets of the corporate debtor, other than the ordinary course of business if it results in a better realisation of value.

Capital gains on transfer of capital assets are treated as taxable transfers unless exempt under section 47 of the Act. Under the SICA regime, the Board for Industrial and Financial Reconstruction (BIFR) exempted sick companies from applying capital gains provision on transfer of land if such a company is managed by its workers' co-operative. However, IBC does not provide such an exemption for transferring a business unit on a slump price or piecemeal sale of assets of the corporate debtor. Being under stress, the corporate debtor may not have immediate cash available to settle tax liability arising on account of such restructuring.

Carry forward of tax holiday benefits

Under NCLT's order, the resolution plan may provide for merger or demerger or even a slump sale in relation to the corporate debtor. Section 80IA of the Act provides certain tax holiday benefits to 'undertakings' engaged in businesses comprising infrastructure, telecom, and industrial parks. Such undertakings availing tax holiday benefits, are not eligible to claim the balance period when they are transferred to another entity following a merger or demerger, but can be allowed to do so when carve-out is undertaken through a slump sale.

Following the transfer of an undertaking, non-continuation of tax holiday benefits may affect the resolution process for corporate debtors under the Code. This may lead to dis-incentivising acquirers of such undertakings. It should be ensured that while implementing a resolution plan needing a merger or demerger, the attributes inherent in the undertaking (eligibility to claim a tax holiday for the residual period) should not be lost.

Whether the period of the corporate debtor being non-operational should be included in the period designated for tax holiday purposes is another issue that needs clarity. The corporate debtor focuses on building a resolution plan to revive the business, rather than carrying out operations. Loss of such periods covered under tax holiday may cause financial distress.

Carry forward of tax losses and unabsorbed depreciation in case of slump or itemised sale

Under IBC, the resolution process may provide for internal restructuring of multiple businesses of the company and/or hive-off of undertakings by selling an undertaking or its specific assets.

Section 72A of the Act provides for various conditions to carry forward and set-off business tax losses and unabsorbed depreciation following a merger or demerger of an industrial undertaking (as defined therein), hotel or ship business, banking company or a public sector aviation company.

Companies undergoing CIRP are usually the ones experiencing business failures (resulting in losses and pressure on servicing debt) and may require to undergo a comprehensive restructuring exercise. From a practical/commercial standpoint, such transferor companies may not be covered under the benefit provided under section 72A for carry forward of losses as the resolution plan may entail sale of non-core assets and/or sale or intermittent shut down of excess capacity after restructuring (breaching specified conditions). Under SICA, BIFR exempted sick companies from applicability of provisions of section 72A of the Act. However, no such exemptions have been provided under IBC. If accumulated losses are not available to be offset, this would result in inequitable treatment on the company undergoing CIRP and various stakeholders who have lost money in the turnaround process of the company. It is only fair that old losses are offset before taxing profits.

Considering that the undertaking's business needs to be restructured through mergers, demergers or slump sale, achieving these objectives should not take away the undertaking's ability to offset losses that necessitated the resolution process.

Reversal of deduction of capital expenditure when assets are sold in less than eight years

Section 35AD of the Act provides for the deduction of capital expenditure incurred wholly and exclusively by specified businesses. If the asset is used for other purposes or disposed off within eight years, the deduction stands withdrawn. Earlier, exemption was provided from applying this claw-back provision under SICA.

The Code currently does not provide any relief to the company from generating cash by disposing of excess capacity.

Deductibility of insolvency resolution process costs

Insolvency resolution process costs include costs of restructuring and of running day-to-day business. Under the Act, costs incurred on amalgamation or demerger are allowed as deduction over five years. Insolvency resolution process costs are incurred on the turnaround of the corporate debtor. It will be worthwhile that the tax department issues clarification on whether these costs would be deductible as revenue expenditure or not.

Submission of return of losses

Per the provisions of the Act, if a taxpayer fails to file its return of income (ROI) within the specified due date, the losses of the relevant previous year shall lapse and not be allowed to carry forward.

Corporate debtors may face difficulty in filing the ROI within the stipulated time due to ongoing proceedings. Therefore, they may face challenges as they will not be able to carry forward the previous year's losses.

An appropriate amendment to the said section, which allows for a delayed filing of ROI by the companies undergoing CIRP, would provide relief to the already distressed companies.

Moratorium period

During the moratorium period, judicial proceedings for recovery, enforcement of security interest, sale or transfer of assets or termination of essential contracts cannot take place against the debtor. This order of moratorium remains in effect until the completion of the CIRP, if NCLT approves a resolution plan or passes a liquidation order for the corporate debtor. The applicability of moratorium to income tax proceedings has been under discussion. Certain rulings have clarified the issue.

In the case of *Monnet Ispat, Supreme Court*[9] upholding the Delhi High Court's order stated that moratorium under the provisions of IBC, shall apply to the tribunal's orders related to the assessee's tax liabilities. The High Court's order also stated that income-tax authorities may revive proceedings, subject to the further orders of NCLT.

In the case of *Kitply Industries Ltd. vs. ACIT*[10], the NCLT Guwahati bench upheld that the income tax department cannot continue proceedings during the moratorium period. The courts acknowledged that the tax authority's interest needs to be protected; a CBDT clarification on the issue would eliminate any ambiguity.

NCLT's powers and IBC's overriding effect

In the resolution case of *Synergies Dooray Automative Limited,* the resolution plan included huge income tax benefits. In August 2017, NCLT approved the plan without providing any comments on such benefits asked. Subsequently, NCLAT, on an appeal by tax departments in March 2019, held that statutory dues, such as income tax and value added tax, come within the meaning of 'operational debt' and tax authorities are to be treated as 'operational creditors'. Under the Code, after NCLT's approval, a resolution plan is treated as binding on all creditors. Consequently, the tax department had to accept the waiver from taxes even when they were not made a party to the proceedings. The department may file an appeal before the Supreme Court against NCLAT's order.

In the resolution case of Amit Spinning Industries, concluded in July 2018, NCLT rejected the proposals included in the resolution plan on termination of ongoing tax litigations.

In the absence of express enabling provisions under the Code or the Act granting jurisdiction to NCLT to decide on tax issues, tax authorities may challenge NCLT or NCLAT order on providing tax reliefs to the corporate debtor under the resolution plan. Some experts think that as section 238 of the Code provides for an overriding effect over other laws, the tax department cannot question any rights provided under the resolution. While overriding provision has been provided in the IBC, tax laws lack enabling provisions for cases other than liquidation corroborating the stalling of any proceedings if moratorium is in motion under IBC and under Section 82 of the Central Goods & Services Tax Act (which specifies that GST payable shall be a first charge on the property, except the provisions of IBC).

Obtaining no objection certificate (NOC)

Section 281 of the Act specifies creation of any charge or transfer of assets by a person to be void against any claim in respect of any tax or any other sum payable by the assessee due to the completion of any proceeding under the Act. However, the creation of charge or transfer will not be treated as void if it is made for adequate consideration and without a notice of the pendency of any proceeding; or with the previous permission of the Assessing Officer.

The section's objective is to safeguard the tax authorities from unscrupulous assessees, who part with their assets to avoid paying taxes. Tax authorities can treat these transactions as void against the claims in respect of tax determined from the transferor in a proceeding that was pending at the time of transfer. The section gives

9. Appeal No 6483/ 2018.
10. 102 taxmann.com 116 (NCLT - Guwahati).

tax authorities power to treat asset transfers as void against their claims.

To protect the buyer's interest, confirming whether IBC supersedes the above power of tax authorities is imperative. Corporate debtors may fail to obtain such NOC in the absence of sufficient cash reserves to pay its tax obligations and inability to offer any guarantee to tax authorities. However, transferring any asset before obtaining such NOC might invite the application of section 281 of the Act.

Similarly, section 81 of the CGST Act requires clearance before transferring any assets against indirect tax claims. Further, it needs to be analysed whether authorities from one state have jurisdiction to declare a transaction undertaken in another state as void and recover the dues from the property located in other states, under the GST law. Clarity on this matter is needed. However, the language of provisions under the GST law of Delhi and Maharashtra seems to suggest that an asset or property transfer may be declared as void. Hence, other states may also have power to recover their GST dues from the property located in other states.

Liability of directors for payment of company's taxes

Section 179 of the Act provides that every director is jointly and severally liable for paying tax dues in case of private companies undergoing liquidation, unless the director proves that non-recovery cannot be attributed to any gross neglect, misfeasance, or breach of duty on his/her part. Whether the company's directors should be held liable for tax dues during liquidation, is under debate.

Applicability of General Anti-Avoidance Rules (GAAR)

Restructuring or acquisition can be done in a tax-efficient manner to save funds for its revival. An arrangement under IBC may be considered an impermissible avoidance agreement and tax consequences may arise if the arrangement leads to significant tax benefits. However, per a CBDT circular[11], GAAR will not apply to an arrangement for which a court or NCLT has explicitly and adequately considered the tax implication.

Per the provisions in ITA, the tax department has power to seek information from any person, bank, company, and other institution that could be useful for an inquiry under the Act. The department has started asking for the resolution plan's details, including status and identification of creditors and debtors under the Code, to investigate possible tax avoidance, thereby exploring the opportunity of invoking GAAR.

Conclusion

IBC was enacted for the timely resolution and maximisation of value of stressed entities' assets, while balancing stakeholders' interests. Tax risks arising due to restructuring under resolution plans challenge the Code's effectiveness and lowers the recovery for creditors from corporate debtor's assets.

It is reasonable to deduce that the government is headed in the right direction, and will bring necessary clarifications and changes in other laws to ensure smooth operation of the IBC.

11. Circular no. 7 of 2017 dated 27 January 2017.

THE DASTUR ESSAY COMPETITION 2019

Sanchi Dhamija

"Feminism: A Misunderstood Concept Today"

Abstract

The global cosmetic products market was valued at around USD 532 billion in 2017 and is expected to reach approximately USD 863 billion in 2024.[1] Recently, the make-up industry was bashed and bludgeoned exposing it to be a mere sham inculcating generations worth of self-loathing and self-consciousness in young women who are nonchalantly expected to appear in a certain manner in public in order to look presentable. However, historical records show that ancient Egyptian women felt empowered through the usage of cosmetic products of their time and age, which also dictated their status in the society. Feminism disguises itself in a coherent and lucid definition but has spread its ambit to cover numerous issues which emerge as the society progresses forward. From the movements to attain political suffrage to the movements propagating nudism, the definition of feminism has spread its wings and sprung across generations to expand its meaning in furtherance of fulfilling the inner awakenings of women now and then. However, there are other certain misunderstood concepts around feminism today which have callously drawn away attention from the paramount necessities of the movement as a whole. Through the following essay the author has undertaken to define and draw out the ambit of feminism directing to its roots and causes, and its journey over generations.

Introduction

"To those accustomed to privilege, equality feels like oppression.'[2] The Merriam-Webster dictionary defines feminism as *'the theory of the political, economic, and social equality of the sexes, an organized activity on behalf of women's rights and interests.'*[3] Etymologically, a man by the name of Eugenie Potonie-Pierre is said to have coined the term feminism in 1896, whilst writing about the indelible link between women's status and social progress.[4] It was during the 1890s that 'feminism' in the sense of women-led activism for equality became a common term, migrating from France and entering the English language as early as October 1894 in a London newspaper article.[5] The theory of feminism itself emerged as early

1. https://www.globenewswire.com/news-release/2018/06/22/1528369/0/en/Global-Cosmetic-Products-Market-Will-Reach-USD-863-Billion-by-2024-Zion-Market-Research.html <accessed on 13th February 2019>.
2. Anonymous.
3. https://www.merriam-webster.com/dictionary/feminism <accessed on 13th February 2019>.
4. In Rosalie Schoenflies et al., eds., Der Internationale Kongress fur Frauenwerke und Frauenbestrebungen: Berlin, 19-26 September 1896 (Berlin: Walther, 1897), 40.
5. Joan Kelly, "Early Feminist Theory and the Querelle des Femmes," Signs 8, no. 1 (Autumn 1982): 4-28; reprinted in Women, History, and Theory: The Essays of Joan Kelly (Chicago: University of Chicago Press, 1984).

as 1794 in publications such as *'A Vindication of the Rights of Woman'* by Mary Wollstonecraft, *'The Changing Woman', 'Ain't I a Woman', 'Speech after Arrest for Illegal Voting',* etc.[6] The moot question then arises is that did feminism not exist as a concept before it was defined and curated through words?

The History of Feminism: Balance of Inconvenience- Shift From Egalitarian To Patriarchal Societies

Our prehistoric forebears are often portrayed as spear-wielding savages, but the earliest human societies are likely to have been founded on enlightened egalitarian principles, according to scientists. A study has shown that in contemporary hunter-gatherer tribes, men and women tended to have equal influence on where their group lives and who they live with. The findings challenge the idea that sexual equality is a recent invention, suggesting that it has been the norm for humans for most of our evolutionary history. The authors argue that sexual equality may have proved an evolutionary advantage for early human societies, as it would have fostered wider-ranging social networks and closer cooperation between unrelated individuals. The study suggests that it was only with the dawn of agriculture, when people were able to accumulate resources for the first time, that an imbalance emerged. It was more beneficial for men to start accumulating resources and more favourable to form alliances with male kin.[7] Thus, the first shift from an egalitarian to a patriarchal society emerged when homo-sapiens shifted their nomadic hunter-gatherer lifestyle to a settled agricultural life.

Fight for Equality

However, many female rulers yet managed to subsist through history. The first female ruler in ancient Egyptian history, Merneith, lived during the reign of the First Dynasty, around 2970 BC.[8] In the literature of the early Vedic period, there are several mentions of female scholars like Lopamudra, Maitreyi and Gargi. Among the educated women of the era, Gargi Vachaknavi is believed to be a pioneer. In the *Brihadaranyaka Upanishad,* she has been credited for having drawn forth from philosophers some of the most profound questions of Vedanta – the nature of the Soul (*Brahman*) and the origins of the universe – during a public debate with Vedic philosopher Yajnavalkya. Queen Didda, who had a leg disability, ruled Kashmir with an iron hand for more than four decades during the 10th century. Her tremendous political survival skills, her ability to rule and her achievement of stability in the fractious kingdom she had inherited is why she is sometimes called the Catherine of Kashmir, referring to the ruthless Catherine the Great (the longest ruling female leader of Russia). When taunted by Mughal commander Wajir Khan about the weakness of women in the battlefield, Bibi Dalair Kaur is believed to have replied fiercely with the following words: "We are the hunters, not the hunted. Come forward and find out for yourself!" At a time when people hardly acknowledged the grievances of women in India, Savitribai Phule, along with her husband Jyotirao Phule, fought injustices against women. In those days, widows used to shave their heads, wear a simple white sari and live a life of austerity. It was Savitribai who decided to stand up against this practice and

6. Moira Ferguson, ed., First Feminists: British Women Writers, 1578-1799 (Bloomington: Indiana University Press, 1985); Simon Shephard, ed., The Women's Sharp Revenge: Five Women's Pamphlets from the Renaissance (New York: St. Martin's, 1985).
7. https://www.theguardian.com/science/2015/may/14/early-men-women-equal-scientists <accessed on 13th February 2019>.
8. https://www.ancient-origins.net/history-famous-people/feminism-and-battle-women-s-rights-ancient-egypt-005895 <accessed on 13th February 2019>.

organized a strike against the barbers in order to persuade them to stop shaving the heads of the widows, most of whom were still children. She also noticed the plight of sexually exploited women who, after becoming pregnant, either committed suicide or killed the newborn due to fear of banishment by society. To cater to such women, she opened a care centre (called Balhatya Pratibandhak Griha or Infanticide Prohibition House) for pregnant rape victims and helped deliver their children. She also founded the first school for women at Bhide Wada in Pune in 1848. Rabindranath Tagore's sister, Swarnakumari Devi, was a committed social worker and started an initiative, Sakhi Samiti, in 1896 to help widows, orphan girls and poverty stricken women of Bengal. She also played an active role in the Indian nationalist movement. The era also saw the rise of many women's organizations like the All India Women's Conference (AIWC). Women within the national movement had begun insisting on greater political and economic participation. These pioneering organizations included the Bharat Stri Mandal in Calcutta, formed in 1910 by Sarala Devi, and the Women's India Association founded in 1917 by Annie Besant, Dorothy Jinarajadasa, Malati Patwardhan, Ammu Swaminathan, Mrs. Dadabhoy, and Mrs Ambujammal. Annie Besant also led the Home Rule League and was elected President of the Calcutta Congress session in 1917. The year 1917 was also significant as Sarojini Naidu led a delegation of women to meet the Montagu-Chelmsford Committee to demand a series of reforms in the condition of Indian women. In 1925, Sarojini Naidu was elected President of Indian National Congress, the first Indian woman to hold that post.[9]

Political Suffrage

The campaign for women's suffrage began in earnest in the decades before the Civil War. During the 1820s and 30s, most states had extended the franchise to all white men, regardless of how much money or property they had. At the same time, all sorts of reform groups were proliferating across the United States–temperance leagues, religious movements, moral-reform societies, anti-slavery organizations–and in many of these, women played a prominent role.

Meanwhile, many American women were beginning to chafe against what historians have called the "Cult of True Womanhood": that is, the idea that the only "true" woman was a pious, submissive wife and mother concerned exclusively with home and family. Put together, all of these contributed to a new way of thinking about what it meant to be a woman and a citizen of the United States.[10]

Anti-Slavery Movement

Anti-slavery and temperance movements sowed the first seeds of feminism in the mid-1800s. In 1840, Elizabeth Cady Stanton and Lucretia Mott were denied seats at the World Anti-Slavery Convention in London due to their gender. Rallying other socially minded people together to discuss the status of women, Stanton and Mott organized the Seneca Falls Convention in 1848. The Declaration of Sentiments, penned by Stanton, outlined the need for equality among men and women, including voting rights. From there, the suffrage movement progressed, with women including Susan B. Anthony and Sojourner Truth leading the way.[11]

9. Singh, S. & Singh, P. (2011). "Shobha De: Deconstructed for Maverick Feminism." In Contemporary Indian Women Novelists in English, Ed. Indu Swami, Sarup: Delhi.
10. Olive Banks, Faces of Feminism: A Study of Feminism as a Social Movement (New York: St. Martin's, 1981).
11. Alison Jaggar, Feminist Politics and Human Nature (Totowa, N.J.: Rowman & Littlefield, 1983).

Women's Liberation Movement

After World War II, a growing number of women pursued higher education and entered the workforce, but they weren't scampering to the tops of career ladders or bursting through glass ceilings. The Women's Liberation Movement of the late 1960s and 1970s therefore emerged from women's desires to revolutionize the fundamental aspects of female life at that time: domesticity, employment, education and sexuality.

National Organization for Women (NOW)

In 1966, Betty Friedan and other prominent feminists formed the National Organization for Women (NOW). NOW became the umbrella organization for many feminist causes, uniting older, college-educated, predominantly white women. These second-wave feminists, such as Ms. magazine founder Gloria Steinem, pushed for access to the pill, abortion, equal employment opportunity, reduction of violence against women and more. Two years later, in 1968, the first national feminist conference took place in Chicago.[12]

Black Feminism

The Women's Liberation Movement was criticized by some feminists, both black and white, for its exclusion of nonwhite, working class women. Although the omission wasn't intentional, this fracture spurred the rise of black feminism. Since Women's Liberation platforms focused solely on gender without the context of race and class, they weren't entirely relevant to all black women. Womanism is one offshoot of black feminism that also developed in the 1970s, coined by Pulitzer Prize-winning author Alice Walker. In the gap between white feminism and black feminism, womanism sought to provide a theoretical bridge by examining society as a universal whole rather than the problems and issues unique to its separate parts.[13]

Anti-Porn Feminism

Anti-porn feminism arose in the late 1970s, pioneered by Catharine MacKinnon and Andrea Dworkin. At that time, pornography had become more readily accessible, and to some feminists, the overtly sexual portrayal of women violated their civil rights and promoted sexual violence. Anti-porn feminist Robin Morgan put it bluntly: "Pornography is the theory, rape is the practice". According to anti-porn theory, heterosexual intercourse is a form of male domination and must be totally altered in a way that it isn't harmful to women.[14]

Pro-Sex Feminism

Sex-positive feminism, also known as pro-sex feminism, surfaced in the early 1980s. These feminists, including Betty Dodson and Gayle Rubin, sought to reclaim heterosexual intercourse as a mutually pleasurable experience for women and men. Sex-positive feminism has evolved to cover not only intimate physical relationships, but also the sex industry, including pornography and prostitution. On the opposite end of the spectrum from anti-porn feminism, some strands of sex-positive feminism consider sex industry work a means of empowerment, not degradation.[15]

Thereby, we can outline the changing dynamics of women in the social and political sphere through the movements they propagated. Where

12. Zillah Eisenstein, The Radical Future of Liberal Feminism (New York: Longman, 1981).
13. Susan Groag Bell and Karen Offen, eds., Women, the Family, and Freedom: The Debate in Documents, 1750-1950, 2 vols. (Stanford, Calif.: Stanford University Press, 1983), 1:2, n. 3, on the decision to avoid anachronistic use of the word "feminism."
14. Barbara Caine, "Feminism, Suffrage, and the Nineteenth-Century English Women's Movement," Women's Studies International Forum 5, no. 6 (1982): 537-50;
15. Leslie Parker Hume, The National Union of Women's Suffrage Societies, 1897-1914 (New York: Garland, 19).

women took crucial decisions and were actively involved in public life in hunter-gatherer societies, to the generations of fighting for basic rights like of property and political suffrage.

Re-Defining Feminism- Extending the Scope

Nudism

One of the most known feminist movements these days is #FreeTheNipple. The general idea is that as men are free to walk the streets bare chested and women should be allowed the same too. The basic debate surrounds around the question 'Why should a women's chest be sexualized and a men's chest not?' It questions the sexualisation of the female body in general in contrast to their male counterparts.

Paying Bills, Financial Independence

It harks back to an era before feminism and gender equality became part of the conversation, when men were usually the sole providers for their families, while most women stayed home to care for the kids. A man who paid for dates showed that he could fill the role of provider, and this supported the model of romantic relationship as transactional, an exchange of money and stability for sex and offspring. The 'Splitting the Bill' movement surrounds around the financial independence of women and their ability to pay for something as basic as food for themselves instead of men paying for the entire bill, which can be taken to be as demeaning.

Portrayal in Movies & Pop culture- Game of Thrones

A look into today's pop culture can give us an overview of the thoughts surrounding around the concept of feminism. The T.V. series 'Game of Thrones' portrays human beings, their relationships with one another, and the social and political structures that help or hinder them, depending on who they are, irrespective of their sex. It is these portrayals of personal and political struggles that give Game of Thrones such a modern feminist tone.[16]

George R. R. Martin, the author of Game of Thrones stated, "Some women hate the female characters. But importantly they hate them as people, because of things that they've done, not because the character is underdeveloped.... Male or female, I believe in painting in shades of grey. All of the characters should be flawed; they should all have good and bad, because that's what I see. Yes, it's fantasy, but the characters still need to be real. To me, being a feminist is about treating men and women the same. I regard men and women as all human–yes, there are differences, but many of those differences are created by the culture that we live in, whether it's the medieval culture of Westeros, or 21st century western culture."[17]

Portrayal In Literature

"I stretched my leg nervously to the other side of the bed to grope for the switch and turned it on. The elephant somersaulted inside the quilt which deflated immediately. During the somer-sault the corner of the quilt rose by almost a foot... Good God! I gasped and plunged into my bed."[18] Ismat Chughtai's allegoric exposition of women exploring their sexuality took the 1942-India by storm in the aftermath of which she was booked for obscenity for bearing the audacity to chronicle the story of sexual awakening of a 'Begum' following her unhappy marriage with a 'Nawab'. Her contemporary Saadat Hasan Manto too got

16. Wilcox, S. (2014, April 28). Women of Westeros. Retrieved from https://www.academia.edu/30038879/Women of Westeros <accessed on 13th February 2019>.
17. Ibid.
18. https://medium.com/@literatureguide/review-summary-and-analysis-of-quilt-by-ismat-chughtai-16ec2293521e <accessed on 13th February 2019>.

into frequent legal feuds with the government for allegedly exuding bawdry through his stories wherein often he talked about ‘taboo’ subjects such as prostitution in a nonchalant manner. Chughtai’s and Manto’s stories often portrayed strong female protagonists who were self-aware enough to take control of their own sexuality and physical desires. Similarly, Nobel Laureate Rabindranath Tagore wrote stories which were way ahead of their time with progressive female characters. Their stories humanized the women they chronicled whilst lurking away from any sort of vulgarity or pruriency. Chimamanda Ngozi Adichie in her book ‘We Should All Be Feminists’ has highlighted about ‘the danger of the single story’, regarding how stereotypes limit and shame our thinking. The word feminist today and the idle of feminism itself has also been restricted in accord to the stereotypical identities assigned to it today.[19]

Separatist And Lesbianism

Separatist feminism is a form of radical feminism that does not support heterosexual relationships. Lesbian feminism is thus closely related. Separatist feminism's proponents argue that the sexual disparities between men and women are unresolvable. Separatist feminists generally do not feel that men can make positive contributions to the feminist movement and that even well-intentioned men replicate patriarchal dynamics. Author Marilyn Frye describes separatist feminism as "separation of various sorts or modes from men and from institutions, relationships, roles and activities that are male-defined, male-dominated, and operating for the benefit of males and the maintenance of male privilege–this separation being initiated or maintained, at will, by women".[20]

Marital Re-Abortion Rights

A recent debate has also emerged with regard to marital and abortion rights of women. Abortion rights partake to involve rights of a woman over her own body and the freedom of choice to determine whether she wishes to carry the child or not. Certain legislations throughout the world have criminalized abortions which are being taken on as being barbaric and demeaning to the lives of women.

The Equal Pay Debate

The Equal pay for equal work debate took to its feet when women started to appear in the public work spaces in huge numbers. The movement is still quite urban in its approach as it partakes to attack on the institutions and establishments where women are inculcated on a pay-roll.

MeToo Movement

'Me Too' or #MeToo is a movement which was initiated in 2006 by a social activist Tarana Burke against the dire concern of the masses on the matter of sexual abuse and harassment in America. The movement started to gain recognition in October 2017 after Alyssa Milano, an American actress posted a tweet asking the victims and survivors of sexual assault to come out, accepting the bitter truth of the society and letting others know that they are not alone. The idea of “Empowerment through Empathy” was behind the Me Too Movement. It was ultimately created to ensure survivors know they're not alone in their journey.[21]

Beauty Pageants

The 1968 Miss America pageant was the backdrop for one of the most iconic events of modern feminism in the United States.

19. https://sol.du.ac.in/mod/book/view.php?id=855&chapterid=538 <accessed on 13th February 2019>.
20. van Zoonen, L. (1994). Feminist media studies. London: SAGE Publications.
21. Evans, Alyssa (2018) "#MeToo: A Study on Sexual Assault as Reported in the New York Times," Occam's Razor: Vol. 8 , Article 3. Available at: https://cedar.wwu.edu/orwwu/vol8/iss1/3.

Members from the New York Radical Women organization demonstrated along the Atlantic City boardwalk against the pageant's perceived misogyny. Protesters threw household items that they believed fostered the collective image of submissive females into a large trashcan.[22]

Thus ironically, feminism didn't begin as an outright quest for gender equality. It evolved from activism for broad social causes to today's spectrum of female-focused theories and philosophies that span topics from education and pornography to race.

Cleaning The Lens: Misunderstandings Surrounding Feminism Today

Feminism however continues to be misidentified and misconstrued. To put it efficiently, feminism is "the advocacy of women's rights on the basis of the equality of the sexes." There are a myriad of issues involved in the movement; sexuality, race, rape culture, transgender rights, the list goes on, but "equality" is the gist of it.

Feminism, its loudest proponents vow, is about fighting for equality. Yet, a lot of feminist rhetoric today does cross the line from attacks on sexism into attacks on men, with a strong focus on personal behaviour: the way they talk, the way they approach relationships, even the way they sit on public transit. Male faults are stated as sweeping condemnations; objecting to such generalizations is taken as a sign of complicity. Meanwhile, similar indictments of women would be considered grossly misogynistic. Feminist male-bashing has come to sound like a cliche – a misogynist caricature.[23] Feminism, its loudest proponents vow, is about fighting for equality. The man-hating label is either a smear or a misunderstanding. This gender antagonism does nothing to advance the unfinished business of equality. If anything, the fixation on men behaving badly is a distraction from more fundamental issues, such as changes in the workplace to promote work-life balance.[24] The 1848 Seneca Falls Declaration of Sentiments catalogued the grievances of "woman" against "man." However, these grievances were directed more at institutions than at individuals.[25] In "The Feminine Mystique," which sparked the great feminist revival of the 1960s, Betty Friedan saw men not as villains but as fellow victims burdened by societal pressures and by the expectations of their wives, who depended on them for both livelihood and identity.[26] That began to change in the 1970s with the rise of radical feminism. This movement, with its slogan, "The personal is political," brought a wave of female anger at men's collective and individual transgressions.[27]

Things have gotten to a point where casual low-level male-bashing is a constant white noise in the hip progressive online media. Take a recent piece on Broadly, the women's section of Vice, titled, "Men Are Creepy, New Study Confirms" – promoted with a Vice Facebook post that said: "Are you a man? You're probably a creep." The actual study found something very different: that both men and women overwhelmingly think someone described as "creepy" is more likely to be male. If a study had found that a negative trait was widely associated with women (or gays or

22. Wartenberg, T. E. (1992). Rethinking power. (T. E. Wartenberg, Ed.) Albany: SUNY Press.
23. https://www.washingtonpost.com/posteverything/wp/2016/06/30/feminists-treat-men-badly-its-bad-for feminism/?utm_term=.1129358a7fba <accessed on 13th February 2019>.
24. https://www.theguardian.com/film/2018/sep/28/female-success-and-male-decline-what-a-star-is-born-tells-us-about-fame-fear-and-feminism <accessed on 13th February 2019>.
25. Esther Kanipe, "The Family, Private Property and the State in France, 1870-1914" (Ph.D. diss., University of Wisconsin-Madison, 1976).
26. On Rereading 'The Woman in America,' " Daedalus [Fall 1987]: 199-210).
27. Sylvia Hewitt's, A Lesser Life: The Myth of Women's Liberation in America (New York: Morrow, 1986).

Muslims), surely this would have been reported as deplorable stereotyping, not confirmation of reality.[28] Meanwhile, men can get raked over the (virtual) coals for voicing even the mildest unpopular opinion on something feminism-related. Just recently, YouTube film reviewer James Rolfe, who goes by "Angry Video Game Nerd," was roundly vilified as a misogynistic "man-baby" in social media and the online press after announcing that he would not watch the female-led "Ghostbusters" remake because of what he felt was its failure to acknowledge the original franchise.[29]

This matters, and not just because it can make men less sympathetic to the problems women face. At a time when we constantly hear that womanpower is triumphant and "the end of men" – or at least of traditional manhood – is nigh, men face some real problems of their own. Women are now earning about 60 per cent of college degrees; male college enrollment after high school has stalled at 61 per cent since 1994, even as female enrollment has risen from 63 per cent to 71 per cent. Predominantly male blue-collar jobs are on the decline, and the rise of single motherhood has left many men disconnected from family life. The old model of marriage and fatherhood has been declared obsolete, but new ideals remain elusive.[30]

Perhaps mocking and berating men is not the way to show that the feminist revolution is about equality and that they have a stake in the new game. The message that feminism can help men, too – by placing equal value on their role as parents or by encouraging better mental health care and reducing male suicide – is undercut by gender warriors like Australian pundit Clementine Ford, whose "ironic misandry" often seems entirely non-ironic and who has angrily insisted that feminism stands only for women. Gibes about "male tears" – for instance, on a T-shirt sported by writer Jessica Valenti in a photo taunting her detractors – seem particularly unfortunate if feminists are serious about challenging the stereotype of the stoic, pain-suppressing male.[31]

Today, when men can lose their jobs because of sexist missteps and be expelled from college over allegations of sexual misconduct, that's a blinkered view, particularly since the war on male sins can often target individuals' trivial transgressions. Take the media shaming of former "Harry Potter" podcaster Benjamin Schoen, pilloried for some mildly obnoxious tweets (and then an insufficiently gracious email apology) to a woman who had blocked him on Facebook after an attempt at flirting. While sexist verbal abuse toward women online is widely deplored, there is little sympathy for men who are attacked as misogynists, mocked as "man-babies" or "angry virgins," or even smeared as sexual predators in Internet disputes.[32]

Feminism- Only For The Urbane?

A critical part of the conversation of feminism is still missing. Indian feminism and feminist issues as they stand, most often, are not fully inclusive of all women or experiences. Indian

28. https://www.washingtonpost.com/posteverything/wp/2016/06/30/feminists-treat-men-badly-its-bad-for-feminism/?utm_term=.1129358a7fba <accessed on 13th February 2019>.
29. https://www.theguardian.com/film/2018/sep/28/female-success-and-male-decline-what-a-star-is-born-tells-us-about-fame-fear-and-feminism <accessed on 13th February 2019>.
30. World Bank. "Engendering Development: Through Gender Equality in Rights, Resources, and Voice". (Oxford: Oxford University Press. 2001.
31. Zeiss Stange Mary and Oyster Carol K. "The Multimedia Encyclopedia of Women in Today's World". (New York: Sage Publications, 2011).
32. Duverger Maurice, "The Political Role of Woman" (Paris : University of Paris, 2010).

feminism has tended to represent the interests and concerns of upper-caste women rather than reflect the experiences of Indian women en masse. By recognising this fact, Indian feminism can more effectively challenge historically entrenched and varied [systems of oppression].[33]

As Indian psychologist Taraasha Chopra explains, "The more education I received, the more aware I became, the conversation on feminism changed. The problems of underprivileged women became nothing more than just facts and figures on a paper. The feminist discourse became more nuanced and we moved on to talking about issues such as socialization, subtle messages of discrimination, rape culture, glass ceilings etc. So the focus of my feminism was more oriented towards the privileged, urban, educated women who were stuck in traditionalist roles while having modern mindsets."[34] Intentional or not, complicity in the face of oppressive systems is choosing the side of the oppressor, which by definition is un-feminist.

Intersectionality is defined as the study of intersecting social identities and the related systems of oppression.[35] First coined within the context of feminism, it examines social hierarchies that privilege and oppress people based on overlapping aspects of their identity such as: race, gender, class, caste, sexual orientation, (dis) ability and so on. For example, two well-known hierarchal systems in India include the patriarchy, based on gender, and the historical caste system. And though the latter no longer formally exists, its norms and repercussions are still very real within Indian communities. When we examine those who are the most vulnerable to each of these systems, women and Dalits, we see the resulting disadvantage is compounded. A severe iteration of oppression specific to these overlapping identities is in the form of sexual violence. Studies show that Dalit women are disproportionately exposed to violence. Beyond this, the conviction rate for rape cases against all women in India is a mere 25%, but when specifically looking at Dalit women the conviction rate drops to an abysmal 2%. Intersectionality goes to understand that when identities intersect the related discrimination can result in an "experience that is more than the sum of its parts.[36]

Feminism thus should also be about dismantling the Kyriarchy, i.e., the social system that keeps all intersecting oppressions in place.[37] If we are not advocating for the women whose realities do not look or feel like our own, then we are unequivocally a part of the problem. Let us understand that different kinds of oppression are interlinked, and that one can't liberate only one group without the others. It means acknowledging kyriarchy and intersectionality–the fact that along different axes, we're all both oppressed and oppressors, privileged and disprivileged.[38]

The key to our liberation is ensuring everyone has an equal chance at success and happiness. It's consciously choosing to be open-minded and inclusive. It's about starting conversations that make us uncomfortable. It's about minimising our role as oppressors, about recusing apathy, as that inevitably hurts us too. It's about viscerally

33. Cohen, Stephen P. (2001). India: Emerging Power. Brookings Institution Press. p. 21.
34. https://www.huffingtonpost.in/shenomics/the-ugly-truth-about-feminism-in-india_a_21632435/ <accessed on 13th February 2019>.
35. Singh, S. & Singh, P. (2011). “Shobha De: Deconstructed for Maverick Feminism.” In Contemporary Indian Women Novelists in English, Ed. Indu Swami, Sarup: Delhi.
36. Gangoli, Geetanjali. Indian Feminisms – Law, Patriarchies and Violence in India. Hampshire: Ashgate Publishing Limited, 2007. Print; pages 10–12.
37. Dhir, Gagan. 1998. ’Man to Women’, Delhi Times, The Times of India, 9 December.
38. Bal, Raka Sinha. 1999. ’Sushma Swaraj: Wife, Mother Politician–A Woman of Our Times’, Life Review, March-April: 10-13.

understanding this simple truth, "I am not free while any woman is unfree, even if her shackles are very different than my own."

A wide range of feminists argued that by grouping together such a wide spectrum of sexual misbehaviour, #MeToo had lost a sense of nuance, deriding the movement as a mere "Twitter feminism", giving the impression that only narcissistic, social media-obsessed millennials want a reckoning over sexual assault. Feminism has thus come to contain two distinct understandings of sexism, and two wildly different, often incompatible ideas of how that problem should be solved. One approach is individualist, hard-headed, grounded in ideals of pragmatism, realism and self-sufficiency. The other is expansive, communal, idealistic and premised on the ideals of mutual interest and solidarity. The clash between these two kinds of feminism has been starkly exposed by #MeToo, but the crisis is the result of shifts in feminist thought that have been decades in the making. In this light, the diversity and breadth of the #MeToo movement is not a weakness, but a strength. After all, if so many women, with so many different kinds of lives, have experienced the same sexist behaviour from men, then it becomes easier to believe that the problem goes beyond individuals and instead relates to wider cultural forces. The ubiquity of sexual harassment means that an individual can't simply avoid it by making the right choices, or by steeling herself with forceful determination; the demand that she do so begins to look absurd.

Call it, then, a conflict between "individualist" and "social" feminisms. In part, the rift is between visions of how to undertake the feminist project, of which tactics are best: whether through individual empowerment, or through collective liberation. But there is a greater moral divide between these two strands of thought, because #MeToo and its critics also disagree over where to locate responsibility for sexual abuse: whether it is a woman's responsibility to navigate, withstand and overcome the misogyny that she encounters, or whether it is the shared responsibility of all of us to eliminate sexism, so that she never encounters it in the first place.[39]

Redefining Feminism: Conclusion

Feminism in present-day India has been showing some encouraging trends. First, increasing economic liberty is allowing women to fight stereotyping. Second, what women want is changing – from economic rights to social and sexual rights. Third, women are not vacating their spaces – they are negotiating harder to expand them. Fourth, there is genuine partnership and collaboration among men and women, particularly youngsters, to embrace meaningful gender equality. Finally, the internet and information revolution is helping women form communities and networks, giving them a bigger voice and tools to organize themselves, forge partnerships and demand their rights.

Most academics attribute the growth of feminism in India to western influence, disregarding the fact that feminism is multicultural – the needs and problems of women who live in different countries are dissimilar. However, Indians did not have to borrow feminism from the West. Throughout history, Indian women have asserted themselves in multiple ways and broken free of oppressive social norms. These whispers of rebellion were bypassed or ignored by patriarchal documentations, but they were always there and they must be remembered. As it has been stated by Chimamanda Ngozi Adichie in her

39. Hebert, L. Camille, Is 'MeToo' Only a Social Movement or a Legal Movement Too? (August 21, 2018). Employee Rights and Employment Policy Journal, Volume 22, No. 2 (2018); Ohio State Public Law Working Paper No. 453. Available at SSRN: https://ssrn.com/abstract=3236309 or http://dx.doi.org/10.2139/ssrn.3236309.

book , “We must raise our daughters differently. We must also raise our sons differently. We do a disservice to boys in how we raise them. We stifle the humanity of boys. We define masculinity in a very narrow way. Masculinity is a hard small cage and we put boys inside this cage.”[40]

The author’s own definition of a feminist is a man or a woman who says, ‘Yes, there is a problem with gender as it is today and we must fix it, we must do better.’ All of us, women and men, must do better. "Liberty, unless enjoyed by all, is unreal and illusory".

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HOT SPOT

Benami Law and Retrospectivity


Amar Gahlot & Sanmati Raonka
Advocates

Analysis of the decision of the Hon'ble Rajasthan High Court in Niharika Jain vs. Union of India – by Amar Gahlot and Sanmati Raonka[1]

New-age laws that seek to remedy economic wrongs are interesting. Economic wrongs could be civil or criminal in character. Clearly, any person who cheats and deprives people of their property is an offender and is a threat to the society at large. He needs to be dealt with through a criminal law. However, another person who breaches a contractual obligation would need to cough up damages and a civil law would be apt and sufficient to deal with this private matter. This simple distinction becomes complex in case of certain economic wrongs – the remedy, whether to be civil or criminal or a mix of both, is difficult to decide.

Legislative approaches

International legislative approaches adopt five methods to counter new-age economic wrongs – criminalization, confiscation, forfeiture, civil recovery, and heavy taxation. Criminalization refers to making the wrong as a punishable offence, while confiscation and forfeiture refer to taking away from the wrongdoer, the result of the wrong or the instrumentalities used in committing such wrong, respectively. These three remedies, undoubtedly, would lie within criminal law. Civil recovery and heavy taxation, on the other hand, are more deterrent and retributive in nature, and fall within the domain of civil law[2].

The recent Indian legislations are inspired by the first two methods – criminalization and confiscation. The money laundering law criminalizes money laundering[3] besides also providing for confiscation[4] of the proceeds of crime. The Benami Act as enacted in 1988[5] ('unamended Benami Act') did not provide

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2. Refer to *Money Laundering Law by Peter Alldridge,* Hart Publishers, ISBN 1-84113-264-0, for an extensive discussion on these five methods.
3. Section 3 of the Prevention of Money Laundering Act, 2002 ('PMLA') defines the offence of money laundering.
4. Section 8 of the PMLA provides that proceeds of crime would be confiscated by the Central Government, if the accused is convicted of the offence of money laundering.
5. Benami Transactions (Prohibition) Act, 1988.

for confiscation, but only criminalized benami transactions. However, in line with the current legislative approach, the law has been drastically amended by the Benami Transactions (Prohibition) Amendment Act, 2016 ('the Amendment Act'). Now, the amended Benami Act also provides for confiscation of benami properties besides criminalising benami transactions.

Decision of the Hon'ble Rajasthan High Court

This shift in remedial approach in the legislation was put to judicial scrutiny recently before the Hon'ble Rajasthan High Court in the case of *Niharika Jain & Ors. vs. Union of India*[6]. The central issue that was put to the Hon'ble Court for decision was that whether the consequences of the Amendment Act were retrospective in nature[7].

The brief facts of the case were that the petitioner had entered into transactions of purchase of lands. These transactions were entered into before 1-11-2016 i.e., the period prior to the coming in force of the Amendment Act. It was alleged by the authorities that these transactions were benami transactions and consequently the said properties were provisionally attached under section 24 of the amended Benami Act. Against the said attachment order, a writ petition was filed challenging the actions of the authorities. Various arguments extended by both the sides, the conclusions of the Hon'ble Court, and their analyses are discussed in seriatim the following paragraphs.

Firstly, the maintainability of the petition was challenged on the grounds of alternate remedy being available. It was argued by the Revenue that the provisional attachment order was still sub-judice before the adjudication authority, whose order in turn was appealable to the Tribunal and the High Court successively. On the other hand, the petitioner defended that in the absence of any appellate mechanism provided in section 24 of the amended Benami Act against the order of provisional attachment, the aggrieved persons have no other remedy for redressal of their grievance but for the writ[8]. The High Court appreciated the contention of the petitioners and that though the authorities under the amended Benami Act are empowered to seek an explanation from the petitioner as to why the property should not be considered a benami property and as to why the provisional attachment of the said benami property shouldn't be done, there is no remedy available to the petitioner to challenge the adverse inference drawn by the authorities basis such explanation[9]. Accordingly, it was held by the Hon'ble Court that where such an order is passed for provisional attachment of the benami property without providing any mechanism for filing an appeal against it, the remedy of writ shall be maintainable.

It is germane to note that the order made by an authority under the Amendment Act is open for an inquiry before the Adjudicating Authority. However, an appeal to the higher forums such as the Tribunal, High Court, etc., is available

6. S. B. Civil Writ Petition No. 2915/2019, order dated 12th July 2019.
7. It is to be noted that the Amendment Act came into force from 1-11-2016, considerably expanding the scope of application of the Benami Act, which had been enacted in 1988.
8. Calcutta Discount Company Limited vs. Income Tax Officer, Companies District, I and Ors. AIR 1961 SC 372; *Raza Textiles Ltd. vs. Income Tax Officer, Rampur (1973) 1SCC 633.*
9. Section 24 of Benami Transactions (Prohibition) Amendment Act, 2016.

only for the specific orders[10]. Thus, the cases wherein the rights and liabilities of an individual are affected by any such order and no appeal provisions are provided under the Act, the writ jurisdiction provided by the Constitution can be invoked[11]. Such a position in law is settled with respect to other similar provisions in the income-tax law[12] and money-laundering law[13] – these provisions also do not contain any appeal mechanism against orders directing a provisional attachment. However, actions taken by authorities are regularly challenged before higher courts by way of writ petitions.

Secondly, the issue of retrospectivity was considered by the Hon'ble Court. It was argued by the petitioner that it was only by way of the Amendment Act that the provisions for confiscation of benami properties were introduced in law. Earlier, a benami property could not be confiscated by the Central Government. Further, since confiscation amounted to a criminal remedy, an amendment bringing such provisions could not be retrospective.

On the other hand, it was argued by the Revenue that the earlier law provided for acquisition without compensation. An analogy could be drawn between the terms 'confiscation' of benami assets as used in the Amendment Act and 'acquisition without compensation', which was provided for in the unamended Benami Act. The Revenue argued that both the terms were similar and as such, there was no new or enhanced punishment that was brought in by the Amendment Act. It was argued that the main object behind the unamended law was to make the act of entering into benami transactions an offence and consequently acquire such benami properties through acquisition without compensation, so that the offender could be divorced from unjust gains and benefits. Hence, keeping in view the intendment and object in introduction of the earlier law, the necessary amendments introduced through the Amendment Act only clarified the intention of legislature. Such intention was to effectively cure and curb the mischief of ever increasing corruption, which was also intended under the unamended Benami Act. Thus, confiscation of the benami property was a mere replacement for acquisition, and was not a new introduction in toto to the benami law.

The Court did not go into much depth of this argument and held these provisions are in nature of substantive provisions which affect the rights of the parties and in absence of any express provision providing for retrospective operation, are prospective in nature. In the backdrop of the objectives sought to be achieved by the Amendment Act, the larger question of substitution of the term 'acquisition' by the term 'confiscation' in the statute and to then determine its penal nature, was not answered by the court and will probably be determined in times to come. Of course, the said analogy must be drawn *qua* the famous *Hayden's rule* while addressing the question of retrospective application of the amended provisions *vis-à-vis* the object sought to be achieved by the unamended Benami Act in order to cure the mischief.

It is also to be noted that though there was a specific provision under the unamended Benami

10. Sections 25, 26, 46, 49 of Benami Transactions (Prohibition) Amendment Act, 2016.
11. Article 32, 226 of the Constitution of India, 1950.
12. Section 281B of the Income-tax Act, 1961.
13. Section 5 of the Prevention of Money Laundering Act, 2002.

Act[14], which provided for acquisition of benami properties without compensation, the same could not have been implemented by the authorities, until the procedure was put in place by the Amendment Act. Thus, in absence of adequate machinery provisions prescribed under the unamended Benami Act, how far would the substantive part be considered useful is another big question left unaddressed by the Hon'ble Court.

Thirdly, the argument on retrospectivity was furthered by the petitioner by questioning as to whether the amendment was declaratory or substantive in nature. It was contended that a declaratory enactment declares and clarifies the real intention of the legislature in connection with an earlier existing transaction or enactment. It does not create new rights or obligations. On the point of retrospectivity of the statute, it was also argued that in absence of contrary intention in the statute, a legislation must be presumed to be prospective. The court contemplated on the techniques which are required to draft a legislation-known as legislative drafting, and as regards to those ones required to understand a legislation which are found in the various principles of 'Interpretation of Statutes'. The court while considering plethora of judgments[15] in accordance with the principle of 'fairness' and the maxim *lex prospicit non respicit*, which means that the law looks forward not backward, held that it is a settled law that a substantive provision unless specifically made retrospective or otherwise intended by parliament should always be held to be prospective.

Lastly, it was argued by the petitioner that the Benami Rules[16] have been notified on 25-10-2016, while the corresponding provision that empowers the Central Government to make such rules has come into force only on 1-11-2016. Thus, it was argued that the rules are bad in law and deserve to be set aside. The Court found substance in such argument. However, the Court did not conclusively opine on this contention and stopped short of setting aside the provisional attachment order on this basis.

It is relevant here to refer to the General Clauses Act, 1897. Section 22 of such Act, which *inter alia* provides for making of rules between passing and commencement of enactment, squarely applies to this argument. The section provides that rule-making power may be exercised any time after the passing of an Act, including even before the Act comes into force. However, rules so framed shall not take effect till the commencement of such Act. The underlying idea behind the section is to enable the formulation of rules which may be needed to bring the Act into operation[17]. Applying this to the present fact matrix, the Benami Rules were notified after the passing of the Amendment Act, but before such Act came into force. This would be perfectly valid as per the General Clauses Act.

Before concluding, it is also noteworthy that this decision serves as a comprehensive judicial referencer on the Benami Law, lucidly explaining the law and rulings on the subject matter. For instance, it points out the distinction between the English Law of Trusts (based on the doctrine

14. Section 5 of the Benami Transactions (Prohibition) Act, 1988.
15. *Sukhdev Singh vs. State of Haryana (2013) 2 SCC 212*; *J. S Yadav vs. State of U.P. & Ors. 2011 6 SCC 570.*
16. Prohibition of Benami Property Transactions Rules, 2016, notified on 2-.10-2016 *vide* GSR 1004(E).
17. *Kishore Singh vs. Revenue Board, Rajasthan AIR 1953 Raj 37.*

of advancement), which is in contradistinction to the Indian law. It also explains the nature of a benami transaction in the Indian context, and its two types – one, wherein there is an operative transfer of title (e.g. where A purchases a property in his own name from the seller B, while the consideration for the same is provided for by C – in this case, there is a real operative transfer happening from B to A), and two, where there is no operative transfer (e.g. where A transfers a property to B without losing on the possession and enjoyment – in such case, there is no operative transfer and A continues to be the real owner)[18]. This is a fundamental distinction and serves as a crucial point to be kept in mind while reading the new Benami Law.

Conclusion

The Amendment Act has been enacted as an aspirational measure. An Act comprising of merely nine sections (the unamended Benami Act) was transformed into a seventy-two-section draconian law[19], through an amending Act, rather than enacting a new law on the subject matter of Benami transactions.

The reasons for 'amending' rather than re-enacting, were explained by the Ministry of Finance to the Parliamentary Standing Committee[20]. It was submitted that a new Bill was drafted and forwarded to the Ministry of Law – under such proposed Bill, transactions entered into between 1988 and present, would also be covered within the purview of the offence of Benami transactions. However, the Ministry of Law opined that such a measure would be violative of Article 20 of the Constitution[21]. The Ministry of Law, therefore, suggested that it would be advisable to comprehensively amend the existing law so that the offences committed during from 1988 to present would also be covered. The Amendment Act, therefore, came into being.

It is pertinent to appreciate the separation of powers enshrined in the Constitution in light of the above context. The only organ of the State which is empowered to decipher the *sententia legis* i.e., the intention of the Legislature behind any law, is the judiciary. The present case evidently establishes this. Despite the intent of the Government behind amending the then existing law on Benami transactions rather than enacting a new law, the Court has held otherwise. The Court has made it abundantly clear that the law, as amended now, would not be applicable to Benami transactions entered into before the Amendment Act came into force. The principle against retrospectivity as laid down in Article 20(1) of the Constitution, has been reiterated, bringing much clarity to current and prospective litigation.

18. *Thakur Bhim Singh vs. Thakur Kan Singh (1980) 3 SCC 72.* Also, see *Meenakshi Mills vs. CIT [1957] 31 ITR 28 (SC).*
19. The Standing Committee of Parliament, which analysed the proposed amendments in great detail, has remarked in its 28th Report that the proposed legislation was 'draconian' – Para 9.2, Page 34 of the Report.
20. Para 5, Page 3 of the Report (*Ibid*).
21. Article 20(1) of the Constitution prohibits laws which punish retrospectively.

DIRECT TAXES

Supreme Court

Keshav B. Bhujle,
Advocate

1 ***Principal CIT vs. Nokia India Pvt. Ltd.***
(2019) 413 ITR 146 (SC) dated 8-4-2019

Appeal to High Court Section 260A – Reopening of assessment – Tribunal holding reopening not valid – High Court dismissing appeal without framing any substantial question of law – High Court should have framed questions and answered the same – Matter remanded: (A.Y. 1999-00)

For the A.Y. 1999-00, the return filed by the assessee was processed u/s. 143(1) of the Income-tax Act 1961. Subsequently a notice u/s. 148 of the Act was issued seeking to reopen the assessment but the proceedings were dropped after the assessee raised objections. A second notice u/s. 148 of the Act was issued. The assessee filed its objections which were rejected by the Assessing Officer and an order of reassessment was passed. The Tribunal held that the reopening was not valid as there was a change of opinion. The Tribunal found that in the letter of the Assessing Officer to the Audit Officer pursuant to the first notice, he had stated that the objection raised by the Department (that the assessee had not increased the book profits by provision made for meeting unascertained liabilities) may be treated as settled as the adjustment mentioned therein was not permissible under the Act.

The High Court dismissed the appeal filed by the Department u/s. 260A of the Act on the ground that it did not involve any substantial question of law within the meaning of section 260A of the Act. The High Court held that in the letter, the Assessing Officer had not only examined the records but come to the conclusion that "there was *prima facie* no evidence that the liabilities were not ascertained liabilities" and that the reopening was based merely on a change of opinion.

The Supreme Court allowed the appeal filed by the Department, remanded the matter and held as under:

"i) The High Court was not justified in dismissing the appeal on the ground that the appeal did not involve any substantial question of law. The following substantial questions of law arise in this appeal and the same should have been framed by the High Court for deciding the appeal on merits:

a) Whether the Income-tax Appellate Tribunal was justified in holding that the notice issued by the Assessing Officer u/s. 148 was bad in law when admittedly the impugned notice was issued in the case where the assessment was made u/s. 143(1) of the Act but not u/s. 143(3) of the Act?

b) Whether the Income-tax Appellate Tribunal was justified in holding that the notice issued u/s. 148 of the Act was bad because based on mere change of opinion by overlooking the fact that there was no foundation to form any such opinion?

c) When admittedly the notice in question satisfied the requirements of section 148 of the Act as it stood, namely, that first, it contained the facts constituting the 'reason to believe' and second, it furnished the necessary details for assessing the escaped income of the assessee, whether the Income-tax Appellate Tribunal was still justified in declaring the notice as being bad in law without taking into consideration any of these admitted facts?

d) In case, if the notice is held proper and legal, whether the finding recorded by the Income-tax Appellate Tribunal on the merits of the case on each item, which is subject matter of the notice, is legally sustainable?"

ii) In our considered view, the aforementioned four questions need to be answered by the High Court on their respective merits while deciding the appeal filed by the Revenue u/s. 260A of the Act.

iii) The impugned order is set aside. The case is remanded to the High Court for answering the aforementioned questions on merits in accordance with law."

2 ***CIT vs. A. A. Estate Pvt. Ltd.***
(2019) 413 ITR 438 (SC); dated 16-4-2019

Appeal to High Court section 260A – High Court without admitting appeal and framing any question of law issuing notice to assessee, hearing parties on questions urged by Department and dismissing appeal – Appeal heard on merits only on questions framed by Court – Not proper – High Court to rehear appeal on merits on questions framed by Court (A.Y. 2008-09)

In this case the High Court affirmed the order of the Tribunal in an appeal filed by the Department. The Supreme Court allowed appeal filed by the Department and held as under:

"i) The High Court did not formulate any substantial question of law as was required to be framed u/s. 260A of the Income-tax Act, 1961. There was a distinction between the questions proposed by the Department for admission of the appeal and the questions framed by the Court. The appeal was heard on the merits only on the questions framed by the High Court under sub-section (3) section 260A of the Act as provided u/s. 260A(4) of the Act. In other words, the appeal was heard only on the questions framed by the Court. If the High Court was of the view that the appeal did not involve any substantial question of law, it should have recorded a categorical finding to that effect saying that the questions proposed by the Department either did not arise in the case or were not substantial questions of law so as to attract the rigour of section 260A of the Act and should have dismissed the appeal in limine.

ii) Instead, the High Court without admitting the appeal and framing any questions of law issued notice of appeal to the assessee, heard both parties on the questions urged by the Department and dismissed the appeal. The assessee had a right to argue "at the time of hearing" of the appeal that the questions framed were not involved in the appeal having recourse to sub-section (5) of section 260A of the Act. But this stage in this case did not arise because the High Court neither admitted the appeal nor framed any question as required under sub-section (3) of section 260A of the Act.

iii) The High Court did not decide the appeal in conformity with the mandatory procedure prescribed in section 260A of the Act. The High Court was to decide the appeal afresh to answer the questions whether the reasons contained in the notice u/s. 148 were relevant and sufficient for issuance of notice dated 22-9-2010, whether any case of escaped assessment within the meaning of section 147 r.w.s. 148 of the Act for the assessment year in question was made out on the basis of the reasons set out in the notice, whether a case of presumption as contemplated u/s. 132(4A) of the Act could be drawn against the assessee on the basis of a document seized in search operation carried in the business premises of another assessee adding a sum of ₹ 1,70,94,000 for determining the total tax liability of the assessee for the year in question as an escaped assessment so as to enable the Department to issue notice dated 22-9-2010 u/s. 148 of the Act to the assessee.

iv) The appeal thus succeeds and is accordingly allowed. The impugned order is set aside. The case is remanded to the High Court for deciding the appeal filed by the Commissioner of Income-tax Mumbai afresh on merits as provided u/s. 260A(4) of the Act to answer the three questions framed by this Court u/s. 260A(3) of the Act."

3 ***CIT vs. Ram Kishan Das***
(2019) 413 ITR 337 (SC) dated 26-3-2019

Assessment – Special audit u/s. 142(2A) – Power of AO to extend time for submission of audit report – S. 142(2C) – Amendment by Finance Act, 2008 inserting words "*sou motu* or" – Clarificatory – AO could extend time for submission of audit report without application by assessee even prior to amendment

Dealing with the retrospectivity of the amendment of section 142(2C) of the Income-tax Act, 1961 by the Finance Act 2008, the Supreme Court held as under:

"i) Sub-section (2A) of the section 142 of the Income-tax Act, 1961 empowers the Assessing Officer to direct the assessee to get its accounts audited by an accountant, on the formation of an opinion that the conditions specified in the provision for recourse to the power are fulfilled. As a necessary incident of this power, sub-section (2C) imposes an obligation on the assessee to furnish the report to the Assessing Officer within the period specified by the Assessing Officer. The substantive part of sub-section (2C) mandates that the report under sub-section (2A) shall be furnished by the assessee to the Assessing Officer within the period specified by the Assessing Officer under the proviso. The Assessing Officer was further empowered, on an application made by the assessee and for any good and sufficient reason, to extend the period further, subject to the stipulation that it shall not exceed an aggregate of 180 days from the date on which the direction under sub-section (2A) has been received by the assessee.

ii) By amendment w.e.f. 1-4-2008 by the Finance Act, 2008 the words "*suo motu* or" were inserted in the proviso before "on an application made by the assessee and for any good and sufficient reasons". The amendment was intended to remove an ambiguity and is clarificatory in nature. The fact that the amendment has been made w.e.f. 1-4-2008 does not detract from it being clarificatory in nature or that it was designed to obviate an ambiguity inherent in the provision as it stood before 1-4-2008. The ambiguity was precisely on the question whether the Assessing Officer was precluded from granting an extension of time of his own accord merely because the assessee was permitted to apply for an extension. Since the purpose of the amendment was to remove the ambiguity, by the Finance Act, 2008, Parliament essentially clarified the position as it existed prior to the amendment.

iii) The provisions of section 142(2C), as they stood prior to the amendment w.e.f. 1-4-2008 by the Finance Act 2008 did not preclude the exercise of jurisdiction and authority by the Assessing Officer to extend time for the submission of the audit report directed under sub-section (2A), without an application by the assessee."

4 *Special Leave Petitions*

4.1 Appeal to Appellate Tribunal – Procedure for admission of additional documents

Supreme Court dismissed the Department's special leave petition against the judgment of the Delhi High Court whereby the High Court held that the Department had to file a formal application under Rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963 to justify the bringing on record of the additional documents in its possession.

Dy. CIT vs. Radhika Roy; (2009) 413 ITR 315 (st): dated 29-3-2019.

4.2 Arm's Length Price – Interest – Whether to be at rate indicated in contract or rate on date of invoice

Supreme Court dismissed the Department's special leave petition against the judgment of the Calcutta High Court whereby the High Court dismissed the Department's appeal from the order of the Tribunal affirming the view of the Dispute Resolution Panel accepting the assessee's contention that for the purpose of determining the arm's length price in a contract with an associate concern it is the rate indicated in the contract which has to be compared to the rate prevailing on the date of the contract rather than the rate prevailing when the invoice is raised.

CIT vs. Ambo Agro Products Pvt. Ltd.; (2019) 414 ITR 1 (st): dated 22-4-2019.

4.3 Business expenditure – Co-operative banks – Deduction for ten per cent of aggregate advances of rural branches whether applies

Supreme Court granted special leave to the assessee to appeal against the judgment of the Kerala High Court whereby the High Court following 365 ITR 343, held against the assessee on the question whether it was entitled to the benefit under the second limb of clause (viia) of section 36(1) of the Income-tax Act 1961 without reference to the definition of rural branch in the *Explanation* (ia).

Ernakulam District Co-operative Bank Ltd. vs. CIT; (2019) 414 ITR 2 (st): dated 25-3-2019.

4.4 Business expenditure – Disallowance u/s. 40(a)(ia) – Payment liable to deduction of tax at source – Interest on delayed delivery of plot whether interest liable to deduction of tax at source

Supreme Court dismissed the Department's special leave petition against the judgment of the Calcutta High Court whereby the High Court held that the Tribunal was right in holding that payment of interest on delayed delivery of plot was not in the nature of interest as defined in section 2(28A) of the Income-tax Act, 1961 and therefore, the provision of section 40(a)(ia) of the Act was not applicable.

Principal CIT vs. West Bengal Housing Infrastructure Development Corporation Ltd.; (2019) 413 ITR 315 (st): dated 5-4-2019.

4.5 Business income – Remission or cessation of trading liability – Waiver of principal loan – Whether sum taxable as income

Supreme Court dismissed the Department's special leave petition against the judgment of the Bombay High Court whereby the High Court dismissed the Department's appeal on the question whether waiver of ₹ 2,96,27,000 of the principal loan constituted a trading liability attracting section 28(iv) and section 41(1)(a) of the Income-tax Act, 1961.

CIT vs. Rieter India Pvt. Ltd.; (2019) 414 ITR 3 (st): dated 9-5-2019:

4.6 Capital gains – Joint development agreement with co-operative society – When transfer takes place and to what extent gains taxable

Supreme Court dismissed the Department's special leave petition against the judgment of the Punjab and Haryana High Court whereby the High Court following 378 ITR 244 held that the Tribunal was justified in holding that no possession had been given by the transferor to the transferee of the entire land in part performance of joint development agreement so as to fall within the scope of section 53A of the Transfer of Property Act, 1882, that in the absence of registration of joint development agreement having been executed after 24-9-2001, the agreement did not fall u/s. 53A of the Transfer of Property Act, 1882 for section 2(47)(v) of the Income-tax Act, 1961 to apply, that the society has transferred the land through the joint development agreement on a *pro rata* basis, that only the money received against which sale deeds had also been executed could be taxed and the money to be received later could not be presently taxed and that the assessee had already terminated the agreement and revoked the irrevocable power of attorney, that sub-clause (vi) of section 2(47) of the Income-tax Act, 1961 would not be applicable.

Principal CIT vs. Chuni Lal Bhagat; (2019) 412 ITR 40 (st): dated 18-2-2019.

4.7 Deduction of tax at source

i) Placement fees and carriage fees paid to cable operators, multi-State operators and direct-to-home operators – whether fee for technical services or payment for work – S. 194J or S. 194C

Supreme Court dismissed the Department's special leave petition against the judgment of the Bombay High Court whereby the High Court following 399 ITR 433 held that the Tribunal was right in holding that the placement fees and carriage fees paid to cable operators, multi-State operators and direct-to-home operators were payments for work covered u/s. 194C and not fees for technical services u/s. 194J.

CIT(TDS) vs. Times Global Broadcasting Co. Ltd.; (2019) 412 ITR 41 (st): dated 25-2-2019.

ii) Royalty – Payment for import of shrink wrapped software/off-the-shelf software

Supreme Court granted special leave to the assessee to appeal against the judgment of the Karnataka High Court whereby the High Court dismissed the assessee's appeal following 345 ITR 494 in which the Court had held that the payments had been made by the assessee to non-residents for having imported shrink wrapped software/off-the-shelf software, that the right that was transferred was the transfer of copyright including the right to make copy of software for internal business, and payment made in that regard would constitute royalty for imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill within the meaning of article 12(3) of the DTAA and the provisions of section 9(1)(vi) of the Income-tax Act, 1961 and tax had to be deducted at source on the payment.

Infineon Technologies India Pvt. Ltd.; (2019) 412 ITR 41 (st): dated 22-2-2019.

4.8 Exemption – Export oriented undertaking – Whether loss of another unit could be set off against profits of unit eligible for deduction

Supreme Court dismissed the Department's special leave petition against the judgment of the Bombay High Court whereby the High Court following 348 ITR 72, dismissed the Department's appeal on the question whether the Tribunal was correct in upholding the order of the Commissioner (Appeals) holding that while computing deduction u/s. 10A of the Income-tax Act, 1961, the loss of another unit of the assessee could not be set off against the profits of the unit eligible for the deduction u/s. 10A.

CIT vs. Russian Pharma Ltd.; (2019) 414 ITR 5 (st): dated 9-5-2019.

4.9 Income – Disallowance of expenditure relating to exempt income

Supreme Court dismissed the Department's special leave petition against the judgment of the Delhi High Court whereby the High Court dismissed the Department's appeal from the order of the Tribunal deleting the disallowance u/s. 14A for the A.Y. 2013-14 for which the assessee did not report any exempt income.

Principal CIT vs. GVK Project and Technical Services Ltd.; (2019) 414 ITR 7 (st): dated 03-5-2019.

4.10 Infrastructure development – Special deduction – Assessee executing road development project under agreement with State Road Development Corporation – Entitled to deduction u/s. 80-IA

Supreme Court dismissed the Department's special leave petition against the judgment of the Gujarat High Court (408 ITR 274) whereby the High Court held that the assessee was entitled to special deduction u/s. 80-IA of the Income-tax Act 1961 in respect of its profits from a road development project, for which, it had entered into an agreement with the Gujarat State Road Development Corporation, a Government agency as defined in section 2(e) of the Gujarat Infrastructure Development Act, 1999.

CIT vs. Ranjit Projects P. Ltd.; (2019) 414 ITR 9 (st): dated 8-4-2019.

4.11 International transactions – Determination of arm's length price – Commission paid to associated enterprise

Supreme Court dismissed the Department's special leave petition against the judgment of the Gujarat High Court whereby the High Court refused to admit the appeal on question whether the Tribunal was justified in directing deletion of the entire transfer pricing adjustment, on the ground that the assessee had given justification for the payment of the commission and why it was at arm's length and that the authority did not bring any comparable case on record to show that the payment of commission by the assessee to the associated enterprise was not at arm's length.

Principal CIT vs. Sun Pharmaceutical Industries Ltd.; (2019) 412 ITR 43 (st): dated 22-2-2019.

4.12 Interest – Liability of non-resident where payer bound to deduct tax at source

Supreme Court granted special leave to the Department to appeal against judgment of the Uttarakhand High Court (309 ITR 85) whereby the High Court held that the assessee, a non-resident, could not be made liable pay the interest u/s. 234B of the Income-tax Act, 1961 as it was the duty of the non-resident foreign company which had engaged the assessee to deduct the tax at source on payment to the assessee.

CIT vs. Tide Water Marine Intl. Inc.; (2019) 412 ITR 38 (st): dated 12-2-2016.

4.13 Search and seizure – Block assessment – Failure to issue notice u/s. 143(2) – Effect

Supreme Court dismissed the Department's special leave petition against the judgment of the Gujarat High Court whereby the High Court held that since the assessee did file the return in response to notice u/s. 158BC of the Income-tax Act 1961, though after a long delay, and the Assessing Officer did not discard it but proceeded on the basis of such return and framed an assessment assessing the income at a figure higher than the returned income, before rejecting such income, notice u/s. 143(2) of the Act was necessary and the Tribunal correctly upheld the judgment of the Commissioner (Appeals) setting aside the assessment for failure to issue notice u/s. 143(2).

Principal CIT vs. Devendranath G. Chaturvedi; (2019) 414 ITR 11 (st): dated 7-5-2019.

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He alone is the really great man whose character is great always, the same wherever he be.

– *Swami Vivekananda*

DIRECT TAXES
High Court

Paras S. Savla, Jitendra Singh, Nishit Gandhi, *Advocates*

1 ***HSBC Holdings PLC vs. DCIT***

Bombay High Court, WP No. 3624 of 2018, Order dt. 1st July, 2019, AY 2011-12

Notice u/s. 148 – Issued by AO placed at Hyderabad – Notice challenged before Bombay High Court – Writ dismissed

The assessee challenged a notice dated 27th March, 2018 issued by the DCIT, Hyderabad u/s. 148 of the Income-tax Act, 1961 for the assessment year 2011-12. A writ petition was filed before Bombay High Court which was opposed by the Department on the ground that the High Court at Bombay had no territorial jurisdiction.

The assessee was a company under the laws of United Kingdom having its registered office in India at Mumbai. Its bank accounts were in Mumbai. The petitioner had filed the return of income for the concerned assessment year at Mumbai and the reopening notice u/s. 148 was served by the Assessing Officer at Mumbai. Hence it was argued that a part of the cause of action had arisen within the limits of Bombay High Court. On the other hand, the Department submitted that the location of the petitioner would not give jurisdiction to the Court to entertain the petition. With the facility of electronic filing of returns, anyone can file the returns from anywhere in the country. Mere place of filing of the return would also therefore not be decisive. The Department contended that the notice was issued by the Assessing Officer situated at Hyderabad. Year-after-year the assessee was assessed by the same authority and it had not raised any objection to be assessed by the said authority. Mere service of impugned notice to the assessee at Mumbai would not mean that any part of the cause of action has arisen within the limits of Bombay High Court. The Departmental representative pointed out that when such a notice is issued by the Department, the same is electronically generated on Income Tax Business Application (ITBA) which in turn gets delivered via e-mail to the e-mail address given by the assessee in the return of income. Additionally, such notices are ordinarily served to the assessee through speed-post. The Court observed that the assessee was being assessed by the Assessing Officer at Hyderabad from time to time. The mere fact that the petitioner has registered office at Mumbai, obviously would not give jurisdiction to Bombay High Court to entertain such a challenge. The Court held that the location of the petitioner obviously cannot be a determinative factor in the context of territorial jurisdiction. Clause (2) of Article 226 of the Constitution provides that powers conferred in the clause (1) to issue directions, orders or writs may also be exercised by any High Court exercising jurisdiction in relation to the territories within which the cause of action, wholly or in part arises for exercise of such power, notwithstanding that the seat of such Government authority is not within those territories. The High Court thus observed that the jurisdiction issue of the High Court is not free from doubt. The Court observed that the assessee is being assessed to tax consistently at Hyderabad. The assessee had a PAN card at such a place. The assessee had never applied for transfer of PAN card. Admittedly, therefore against the assessments that would be made by the DCIT, Hyderabad, appeals would lie before the Appellate Commissioner stationed there. Further appeal at the hands of the aggrieved party would lie before the Income Tax Appellate Tribunal, Telangana. The Court also observed that section 269 of the Act defines the High Court as to mean in relation to any State the High court for that State. Any challenge to the orders of Assessing Officer, Appellate Commissioner or the Tribunal in the present case would lie before the High Court of Telangana (previously High Court of Andhra Pradesh). The Assessing Officer and the Appellate Authorities, therefore, would be bound by the law propounded by the said High Court. The Court further held that in central legislations such as the Income-tax Act, High courts give due respect to the pronouncements of another High Court, in order to avoid difference of opinion in central legislations. On rare occasions diversion of views between the High Courts are inevitable. Thus if a Court entertains a petition merely because a small part of the cause of action may have arisen within the jurisdiction, it would be giving rise to the possibility of different legal principles being applied in case of the same assessee on the same issue and possibly in relation to the same assessment year. For the present case, an appeal against the original assessment (if at all done) for the Assessment Year 2011-12 would be governed by the law laid down by Telangana High Court. In the context of a challenge to the notice of reassessment, the present Court would apply the decisions of Bombay High Court. This would be wholly undesirable. The Court, thus held that even if the contention of the assessee that the facts of the case would suggest arising of a part of cause of action within the jurisdiction of the Court was accepted, in Court was of the opinion that it should not exercise such jurisdiction and instead allow the petitioner to file appropriate petition before the High Court which has jurisdiction over the Assessing Officer at Hyderabad. Under these circumstances, the writ petition was not entertained.

2 ***Competent Authority, Patiala Urban Planning and Development Authority vs. DCIT***

CWP 2009 of 2019, Punjab and Haryana High Court, order dt. 23rd July, 2019

Wrongful attachment and retention of money by the department – Department refunded the amount however denied interest – Interest allowed

There was a tax recovery against Patiala Development Authority. However, the amount belonging to the assessee was also attached. This attachment and recovery of assessee's money were challenged by way of Civil Writ Petition No. 16162 of 2014 which was allowed by the Hon'ble High Court on 17-3-2015 holding that the amount was wrongly attached and the Revenue was directed to refund the same. Though the amount was refunded by the Revenue, they denied interest. The assessee again filed a writ petition seeking compensatory interest for wrongful attachment of the money. The Court observed that the department had accepted that the money was wrongly attached and retained. The revenue denied interest on the ground that there is no provision for grant of interest on any excess income tax which was recovered. The assessee had argued that it would have no objection with this proposition of law which has been sought to be advanced by the Revenue but the present was not a case of recovery of excess tax but a case where attachment and retention of money was made which did not belong to the defaulter but belonged to a different person. This wrongful attachment and retention could never be envisaged under the Income-tax Act and, consequently, the attachment and retention cannot be related to any provision of the Income Tax Act. The interest which has now been sought was on the general grounds of equity and fairness. The Assessee argued that the claim which has now been made at the rate of less than 10% for wrongful retention of money for a period of about 15 months, cannot be said to be excessive by any standards. The Court held that the provision of interest in Section 244A of the Income-tax Act would have no applicability in the present case because it is a case of illegal attachment and retention. However, there can be no escape from the payment of interest. The Court allowed the petition and interest of ₹ 3.68 crore were directed to be paid within two months, failing which further interest @ 9% per annum on the amount would be payable.

3 ***The Majestic Auto vs. CIT***

ITR 602 of 1995, Punjab and Haryana High Court, order dt. 24th July, 2019

Payment for designs – use or supply of design – use of design only after production start – upfront payment for supply not royalty

The assessee had entered into an agreement with Steyr-Daimler-Puch AG (Puch), (Motorized Two Wheel Division), Austria, whereby the latter granted an exclusive and individual Right and licence to use manufacturing information supplied by PUCH to manufacture, assemble and sell in India vehicle Maxi Plus and Super Maxi. As per the Clause No. 1.4 of the agreement, PUCH supplied drawings, designs, specifications, processes, schedule and all other relevant technical details and documents to the assessee for which the assessee paid an amount of 3 million Austrian Schilling in three installments. Further, for the purpose of royalty, the agreement had a separate Clause No. 2.1 as per which after the production started the assessee would pay royalty at a certain percentage on the basis of units produced. It was not disputed that on the royalty paid under Clause 2.1, the assessee was liable to deduct tax at source. The dispute in the appeal was only on whether on the payment of 3 million Austrian schillings the assessee was liable to deduct tax at source. The A.O. held that even for the payment of 3 million Austrian Schilling, the assessee was liable to deduct tax since it was in the nature of royalty payment. This was reversed by the CIT(A) based on DTAA between India and Austria. However, the Revenue carried the matter to the Tribunal. The assessee had argued before the Tribunal that the payment of 3 million was for the supply of material and their use would arise when the vehicles would be started to be produced. It was at that stage when royalty would become payable. The Tribunal, however, allowed the Revenue’s appeal by interpreting the word supply and holding that 'supply' includes 'use'. On further appeal, the High Court reversed the Tribunal order by observing that 'royalty is a payment to an owner for the ongoing use of its assets or property such as patents or natural resources for business purposes. The High Court held that the word 'royalty' has been defined by the Supreme Court in the case of *Entertainment Network (I) Ltd. vs. Super Cassette Inds. Ltd., 2008(3) SCC 30* as the remuneration paid to an author in respect of the exploitation of a work, usually referring to payment on a continuing basis (i.e., 10 per cent of the sale price) rather than a payment consisting of a lump sum in consideration of acquisition of rights. The Court observed that an assessee would have to pay a certain amount of money to PUCH for every vehicle which is sold using its designs. The Court held that the Tribunal has given an unnatural and strained meaning to the expression 'supply'. By entering into the agreement and by supplying the material PUCH authorized its use but its actual use would start only when production and sale commenced and that would be the stage at which royalty would be payable. The High Court thus decided in favour of the assessee.

Note: In this judgment there is no explicit reference to *Explanation 2* to section 9(1)(vi) which defines "royalty". However, as the facts suggest, the judgment interprets the definition of royalty in the context of its taxability u/s. 9(1)(vi) wherein any consideration for use is chargeable to tax as royalty since there could not have been two uses of the same designs/specifications. Attention also needs to be drawn to the fact that no other argument was raised by the Revenue in this case so as to urge that under the other clauses of *Explanation* 2, the said sum could probably be termed as royalty.

4 ***TLG India P. Ltd. vs. ITO (TDS)***
W. P. No. 1788 of 2019, Bombay High Court, Order dt. 29th July, 2019

Payment for advertisement to Google and Facebook – AO undertook a research on the business of the assessee and passed order u/s. 201 treating assessee in default for non-deduction of tax on payments made – Principles of natural justice violated

The assessee company was an advertising and media agency, engaged in the business of advertising by creative and production work, media planning and incidental activities. The central dispute between the assessee and the Income Tax Department was on the question as to whether tax needs to be deducted on payments made to the agencies like Google and Facebook for services provided. According to the assessee, the deduction of tax at source would be made in terms of Section 194C of the Income-tax Act, 1961 ('the Act' for short) as payments to the contractors. The department contended that such deduction should have been made as provided under Section 194J of the Act by way of professional or technical services. The controversy arose pursuant to a spot survey conducted at the registered office of the assessee, during which the statements were recorded under Section 131 of the Act. Summons were issued to the company requiring the production of books of account and other information. The assessee filed a detailed submission before the authority on 5th April, 2018 offering its version and explanation as to why the deduction of tax at source under Section 194C of the Act was proper and that the deduction under Section 194J of the Act was not called for. Further replies and representations of the assessee were brought on record. Eventually, the Income Tax Officer (TDS) passed his impugned orders under Section 201(1)/201(1A) of the Act and held that the Petitioner had short tax deducted/not deducted tax at source to the tune of ₹ 91.10 crore during the impugned assessment years. Interestingly while forming his opinion that tax is deductible u/s. 194J the ITO had done some independent research on his own and formed his opinion on the basis of the said research. However, the Assessee was neither provided a copy of the said research nor even a summary of the findings of the ITO on the basis of his research. Therefore Assessee challenged the orders of the ITO in the writ petition mainly on the ground of breach of principles of natural justice. The Revenue urged and strongly resisted the petitions on the preliminary contention that the impugned orders are appealable and hence the assessee must be relegated to such appeal remedy and writ petition directly challenging the orders, should not be entertained. The Court observed that detailed speaking impugned order was passed by the ITO (TDS) and he had done extensive research on the nature of service provided. The ITO (TDS) had referred extremely to in-depth research carried out by him on the internet to make the various observations. There was nothing in the impugned orders to suggest that he shared such research with the assessee before he passed the final orders. The High Court further observed that in the affidavit in reply the ITO (TDS) tried to suggest that in any case, the assessee was in the same business, was totally aware about the nature of the activity, therefore cannot claim ignorance and since the assessee being well aware of the nature of the services, it was futile to share with the assessee. The Court held that ITO can carry his own research however he should have followed the principles of natural justice. The least that he was expected to do was to share such material with the assessee giving an opportunity to rebut the same if so desired by the assessee. In the result, the orders were quashed only on the ground of natural justice. The Hon'ble High Court remitted the matter back to the ITO to give the Petitioner an opportunity to meet with all the documents/research in his possession on the basis of which the orders were passed against the assessee.

5 ***Sharan Hospitality Pvt. Ltd. vs. DCIT***

ITA No. 557 of 2017, Bombay High Court, Order dt. 1st July, 2019

Annual value of the property u/s. 23(1)(a) – Occupancy certificate was not received - Notional value cannot be computed

The assessee had purchased a commercial property from one M/s. Prime Property Development Corporation Limited under Conveyance Deed dated 18th December, 2008. The intention of the assessee was to let out this property for earning rental income. The building in which this property was situated, was given Occupancy Certificate 'OC', by the local authority on 21st May, 2009, only thereafter the remaining consideration of ₹ 8.75 crore was made. In the meantime, the assessee had leased out the property with effect from 1st April, 2009. Lease Agreement was executed in August, 2009, which also referred to the Lessee being put in possession of the property on 1st April, 2009. While assessing the return of income of the assessee for the assessment year 2009-10, the Assessing Officer was of the opinion that for the period between 1st January, 2009 till 31st March, 2009, the assessee had to pay tax on the rental income of the property in question on notional basis. The Assessing Officer passed an order of assessment on 22nd December, 2011, in which he levied a tax on the sum of around ₹ 1.16 crore. In fact, the Assessee had declared the said amount as notional rent but claimed vacancy allowance for claiming no tax liability. This was rejected by the Assessing Officer on the ground that the same would be available only when the property or any part of the properties let and/or was vacant during the whole year or any part of the previous year, which according to the AO was absent in the present case. The assessee carried the matter in Appeal before the Commissioner. The Commissioner rejected the Appeal. Upon which, the assessee carried out the matter further in appeal before the Tribunal. The Tribunal confirmed the view of the AO and rejected the assessee's appeal, holding that the interpretation of the AO of Section 23(1)(c) of the Act was correct. On further appeal, the High Court observed that it was not necessary to enter into the interpretation of Section 23(1)(c) of the Act, since the issue could be thrashed out on the facts and the first principles emerging from the statutory provisions. The Court held that the OC for the property in question was obtained by the builder only in May, 2009 and, by operation of law, such property could not have been legally occupied by either the Assessee or any other person under the license given by the assessee. It was a different matter that the assessee did execute a lease deed putting the lessee in possession of the property on 1st April, 2009 but assessee explained that it was only for completing the furniture and fixtures and not for occupation for commercial use. The High Court without going into the correctness of such explanation and held that the question of charging tax on notional rental income during such period does not arise. The Court held that between 1st January, 2009 to 31st March, 2009, the property was legally not occupiable and not occupied and thus allowed the appeal of the assessee.

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Tribunal

Neelam Jadhav, Neha Paranjpe & Tanmay Phadke, *Advocates*

Reported Decisions

1 ***Varun Seth vs. Asst. Commissioner of Income Tax, Circle 47(1), New Delhi***

[ITA 1388/Del/2019] (Assessment Year: 2015-16), dated 14-5-2019, [2019] 107 taxmann.com 133 (Delhi-Trib.) Order dated 14-5-2019

Exemption – Section 54 – when the sale consideration received by the Assessee on the sale of a residential flat is invested for acquisition of a plot to construct a residential house, the exemption under section 54 cannot be denied merely because the assessee could not obtain the possession of plot within a period of three years due to failure on the part of the developer to hand over the possession

Facts

The Assessee is an Individual and the assessment year under consideration is 2015-16. During the year under consideration, the Assessee sold a residential plot at Upper Hill Road, Civil Lines, Delhi on 28-11-2014 for the total consideration of ₹ 6,10,50,000/- and declared the LTCG of ₹ 1,92,80,160/- in his return of income. The assessee claimed a deduction of ₹ 1,58,00,000/- u/s. 54 of the Act on acquisition of a residential plot at Noida on 01.06.2013 which in turn was to be utilized for the construction of a residential house and ₹ 25,10,000/- was deposited in the capital gain account. During the course of assessment proceedings, the AO observed that the assessee has not constructed a house within the stipulated time provided u/s. 54 of the Act and has not fulfilled the conditions of the said section. On these observations, the AO disallowed the claim of deduction of ₹ 1,58,00,000/- pertaining to the investment made in a plot which was to be utilized for the construction of a residential house. On appeal, the assessee did not find any success before the CIT(A). Being aggrieved, the assessee preferred an appeal before the ITAT. After hearing both the sides, the ITAT held as under:

Held

The ITAT held that in the present case, the assessee has made an investment of ₹ 1,58,00,000/- for acquisition of a plot which was to be utilized for the construction of a residential house and the remaining amount of capital gains of ₹ 25,10,000/- was deposited in the capital gains account well within the time as provided u/s. 54 of the Act. The ITAT observed that it shows the intention of the assessee to invest in a residential house and avail a deduction u/s. 54 of the Act.

It was also observed by the ITAT that inspite of making the payment, the developer could not hand over the possession of a residential plot to the assessee as he failed to clear the land dues to the extent of ₹ 10,205 crore towards Noida Authority. Thus, there was a reason beyond the control of the assessee due to which the assessee could not construct a residential house within a period as provided u/s. 54 of the Act. The ITAT therefore, held that the amount utilised by the Assessee in the acquisition of a land should be construed as amount invested in purchase/ construction of a residential house. The ITAT held that the intention of the statute as provided in section 54 of the Act has been fully satisfied by the assessee in the present case and therefore, the assessee is entitled for a deduction under section 54 of the Act. While coming to this conclusion, the ITAT relied on the decision of the Supreme Court in the case of *Sanjeev Lal vs. CIT [2014] 365 ITR 389 (SC)*. The appeal filed by the Assessee was allowed.

2 ***Maharashtra State Warehousing Corporation vs. DCIT, Circle -14, Pune***

[ITA 2396 to 2399/Mum/2017] (Assessment Years: 2003-04 to 2006-07), [2019] 107 taxmann.com 92 (Pune-Trib.) Order dated 3-6-2019

Section 72 r.w.s 254 –Business losses computed by the assessing officer while giving effect to the order of ITAT must be carried forward in subsequent assessment years and should be set off against the business income of those years even though the same were not claimed in original returns of income

Facts

The assessee is a state government undertaking, engaged in providing warehousing facilities in the State of Maharashtra. The return of income for the A.Y. 2002-03 was filed by declaring the total income at ₹ Nil/-. The assessment was completed u/s. 143(3) of the Act by assessing the total income at ₹ 5,90,35,236/-. On appeal, the CIT (A) allowed the appeal of the assessee in part. Being aggrieved, an appeal was preferred before the ITAT which was restored back to the AO to recompute a disallowance u/s. 14A r.w.r 8D. The AO thereafter, passed the assessment order dated 14.12-2009 u/s. 143(3) r.w.s 254 of the Act by computing the business losses at ₹ 13,00,25,239/- and further held that the said business losses are allowed to be carried forward and set off. However the CIT did not find the said view correct and revised the order dated 26-3-2012 u/s. 263 of the Act. Being aggrieved, the assessee preferred an appeal before the ITAT wherein the ITAT set aside the order passed by the CIT u/s. 263 of the Act. Pursuant to the same, the assessee filed rectification applications for the years under consideration i.e., A.Y. 2003-04 to 2006-07 requesting the AO to allow the benefit of carry forward and set off of business losses determined by him in the light of the directions given by the ITAT in the A.Y. 2002-03. The said applications were rejected by the AO on the observations that the assessee has not claimed the set off of carry forward of the business losses in the original returns filed for the respective assessment years and the same cannot be allowed at a belated stage. On appeal, the CIT(A) confirmed the action of the AO being aggrieved, the Assessee preferred the present appeals before the ITAT. After hearing both the sides, the ITAT held as under:

Held

The ITAT noticed that the only issue that emerges for the consideration is whether the business losses determined at by the AO while giving effect to the order of the ITAT can be carried forward and the benefit of set off can be allowed against the business income of the subsequent Assessment years in absence of any claim in the original returns of income. It is an undisputed fact that the assessee in the returns of income for the A.Y 2003-04 to 2006-07 has not claimed the set off of brought forward business losses. The said losses were determined by the AO in the assessment year 2002-03 only on the basis of the directions given by the ITAT for the said year. The A.O. passed the order u/s. 143(3) r.w.s. 254 on 14-12-2009 computing the business losses of ₹ 13,00,25,239/- eligible to be carried forward. When the said order was passed, the assessee had already filed the returns of income for the years under consideration. Thus, the assessee had no occasion to claim the set off of brought forward business losses. Further, it was observed that consequent to the order passed by the ITAT for the A.Y. 2002-03, the Assessee has received the relief which has cascading effect on the subsequent Assessment Years and the A.O is duty bound to give effect to the said order in later affected assessments. In view of the same, the appeal filed by the assessee was allowed.

Unreported Decisions

3 ***Shri Ratanlal C. Bafna vs. JCIT***
[MA 97/PUN/2018 in ITA 204/PUN/2012] (Assessment Year: 2008-09), order dated 15-3-2019

Section 254(2) – Rectification of an order is not possible once an appeal against the original order against which a rectification application is filed has already been admitted by the High Court

Facts

The assessee has preferred a Miscellaneous Application (MA.) before the ITAT second time against the order passed in ITA 204/PUN/2012 for the A.Y. 2008-09. In the said application, the assessee agitated that while deciding the appeal, the ITAT did not adjudicate the ground no. 12 pertaining to an opportunity of cross examination raised before it and the same constitutes a mistake apparent from record. The assessee mentioned that he had previously filed a MA against the same order of the ITAT which was dismissed *vide* order dated 27-7-2018. However as per the contention of the assessee, the same would not vitiate the second application since the assessee did not raise the point of non-adjudication of ground no. 12 in his first MA. The assessee relied on the decisions in the case of *CIT vs. Aiswarya Trading Company [2011] 323 ITR 521(Ker.), Hiralal Suratwala vs. CIT 56 ITR 339 (All.)* and *CIT vs. Smt. Vasantben H Sheth [2015] 372 ITR 536 (Guj.)* and explained that the issue which was not subject matter in the earlier MA can be agitated in the second MA. On the query from the bench, it was submitted that the appeal against the quantum order has already been admitted by the High Court *vide* its order dated 26-11-2018. The assessee placed reliance on the decision of Bombay High Court in the case of *R. W. Promotions Pvt. Ltd. vs. ITAT (WP. No. 2238/2014*), order dated 8-4-2015 and requested the ITAT to rectify its order. After considering the arguments of both the parties, the ITAT held as under:

Held

The ITAT held that it is an undisputed fact that against the order dated 31-3-2015, the assessee has preferred an appeal before Bombay High Court which stands admitted by the Court on the substantial questions of law. The ITAT perused the decision relied by the assessee and held that the decision of Bombay High court in the case of *R. W. Promotions Pvt. Ltd. vs. ITAT (WP. No. 2238/2014),* order dated 8-4-2015 is distinguishable from the present case since in that case, while deciding a M.A., an appeal was filed before the High court which was yet to be admitted. However, in the present case, the appeal against the order of ITAT has already been admitted on the substantial questions of law. Further the ITAT referred to the decision Guajrat High Court in the case of *CIT vs. Muni Seva Ashram [2013] 38 taxmann.com 110 (Guj.)* and held that when an order of the ITAT is subjected to an appeal before the High Court and the same is admitted on substantial question of law, the ITAT cannot recall its order. In the light of the same, the ITAT rejected the contentions of the Assessee and dismissed his application.

4 ***Pankaj Bhotika vs. ITO***

[ITA 1710/Kol/2018] (Assessment Year: 2009-10), order dated 24-7-2019

Section 271B – Penalty cannot be levied when the assessee was not guided properly by his professional consultant and being the first year of the business, did not realize the fact that he was required to get his books of account audited since his gross turnover had exceeded the monetary limits prescribed u/s. 44AB of the Act.

Facts

The assessee is an individual and the issue is with regard to a levy of penalty u/s. 271B of the Act. For the assessment year 2009-10, the assessee initially filed a return of income declaring the total income at ₹ 1,29,070/-. The said return was processed u/s. 143(1) of the Act. Thereafter, on the receipt of the information from the investigation wing, the return was selected for the reassessment proceedings. During the course of the said proceedings, the assessee submitted a revised computation of income along with the financials of his proprietorship business. From the said financials, it was observed that despite the fact that the gross turnover of the assessee is ₹ 1,46,14,105/8- which exceeded the monetary limits mentioned u/s. 44AB of the Act, the assessee did not get his books of account audited for the year under consideration. The AO issued a show cause notice to the assessee to which the assessee filed his reply stating that due to lack of knowledge and proper advice, he could not comply with the requirements of the said section. However, the aforesaid reason did not impress the AO and the penalty of ₹ 73,070/- was levied u/s. 271B of the Act. Being aggrieved, the assessee filed an appeal before the first appellate authority but did not succeed. Later on, an appeal was filed before the ITAT. During the course of hearing, it was argued on behalf of the assessee that this being the first year of the business, the assessee due to lack of knowledge and proper advice failed to get his books of account audited for the year under consideration. It was further submitted that the assessee was totally dependent on his accountant who suggested him not to get his books of account audited for the present year. On the aforesaid submissions, the assessee requested the ITAT to delete the said penalty. Whereas on the other hand, the Revenue objected to the said submission and requested the ITAT to confirm the order of the CIT(A). After hearing both the sides, the ITAT held as under:

Held

Firstly, the ITAT noted the legal position regarding the levy of penalty. The ITAT observed that the penalty for a failure to carry out a statutory obligation is the result of quasi-criminal proceedings and it will not be levied unless the party obliged, either acted deliberately in defiance of law or was guilty of conduct contumacious or dishonest or acted in conscious disregard of its obligation. It is further observed by the ITAT that a penalty will not be imposed merely because it is lawful to do so. While coming to the said observation, the ITAT referred to the decision of the Apex Court in the case of "*Hindustan Steel Ltd vs State of Orissa [1972] 83 ITR 26 (SC)*". Coming to the facts under consideration, the ITAT observed that the assessee was not advised properly. It further observed that it is the first year of the business of the assessee and he was misguided by his accountant. On the above mentioned factual observations, the ITAT accepted the contention of the assessee and deleted the penalty levied us 271B of the Act by relying on the decision of its Co-ordinate bench in the case of *Ramesh Kumar vs. ITO (ITA No: 454/*

Asr/2017). Finally, the appeal filed by the Assessee was allowed.

5 ***Rasai Properties Pvt. Ltd. vs. DCIT***
[ITA 770/PUN/2018] (Assessment Year: 2013-14), order dated 28-6-2019

Section 271(1)(c) – Penalty cannot be levied when a mistake committed by the assessee is genuine and the assessee has no intention either to conceal particulars of its income or to furnish any inaccurate particulars of income

Facts

The assessee is a private limited company and had filed its return of income for the assessment year 2013-14 on 27-9-2013 declaring the total income at ₹ 80,19,650/-. The said return was selected for the scrutiny assessment. During the course of assessment proceedings, the AO observed that the assessee had taken a deduction of ₹ 67,00,000/- from the block of assets comprising of tangible fixed assets which formed a part of the balance sheet. Pursuant thereto, the AO asked the assessee to explain as to why it had not offered the income from the sale of aforesaid properties under the head income from capital gains. In response, the assessee furnished the working of the capital gains amounting to ₹ 19,45,176/- and offered the same to tax. While concluding the assessment proceedings, the AO initiated penalty proceedings u/s. 271(1)(c) of the Act and finally levied the same. Being aggrieved by the stand taken by the AO, the assessee preferred an appeal before the first appellate authority but did not succeed. Thereafter, an appeal was preferred before the ITAT. In the course of hearing, it was submitted that there was no *mala fide* intention on the part of the assessee regarding its failure to offer the said capital gains in the original return income. It was submitted that after knowing about the said error, the assessee immediately offered the capital gains to tax during the course of the assessment proceedings. In the light of the aforesaid submissions, the assessee requested to delete the penalty levied by the AO u/s. 271(1)(c) of the Act. On the other hand, it was submitted on behalf of the Revenue that the said capital gains would remain untaxed if the case of the assessee had not been selected for the scrutiny assessment. After hearing both the sides, the ITAT held as under.

Held

The ITAT observed that though the said capital gains were not offered to tax in the original return income, the assessee had duly disclosed a deduction of ₹ 67,00,000/- pertaining to the sale of the three shops from the block of assets in its Balance Sheet for the year under consideration. Further, the assessee after realizing its mistake offered the said capital gains during the course of the scrutiny assessment proceedings. The ITAT observed that the mistake committed by the assessee is genuine and the assessee had not intended or attempted to either conceal its income or furnish inaccurate particulars calling for a levy of penalty u/s. 271(1)(c) of the Act in the facts under consideration. While coming to aforesaid conclusion, the ITAT referred to the decision of the Apex Court in the case of *PriceWaterHouse Cooper Pvt. Ltd. vs. CIT (2012) 348 ITR 306 (SC).* On the above mentioned observations, the ITAT deleted the said penalty and allowed the appeal of the assessee.

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INTERNATIONAL TAXATION
Case Law Update

CA Tarunkumar Singhal & Sunil Moti Lala,
Advocate

A. HIGH COURT

1 ***Epcos Electronic Components S.A vs. Union of India***

[2019] 107 taxmann.com 227 (Delhi) – W.P. (C) No. 10417 of 2018

Revision petition under section 264 before CIT seeking rectification of return in respect of which intimation is sent under section 143(1) for taking benefit of Most Favourable Nation clause is maintainable

Facts

1. The assessee a company incorporated in Spain earned service fees for providing management related services to EIPL, an Indian Company. The assessee filed return offering the same for tax @ of 20% plus surcharge and education cess under Article 13 of the DTAA between India and Spain. The AO by an intimation dated 10th March, 2016 under Section 143(1) of the Act processed the return of income.

2. The assessee, later realised while referring to Article 13 of the DTAA that it had failed to refer to Clause 7 of the Protocol appended to the DTAA which is an integral part and parcel of the DTAA. According to the terms of the protocol, further concessional rate of tax was to be charged in terms of the agreement between India and another member of the OECD, by India after 1st January 1990, wherein India limits its taxation on FTS to a rate lower than that provided in Article 13 of the DTAA, then the said rate shall apply under the DTAA to the assessee as well.

3. This led the assessee to file the revision petition under Section 264 of the Act seeking to revise the order under Section 143 (1) of the Act claiming it to be prejudicial to the Petitioner's interest as the rate of tax should be 10% and not 20% for the FTS earnings, as the DTAA between India and Sweden was entered into on 25th December, 1997 i.e., more than two years after the DTAA between India and Spain which provided for the tax on FTS at 10%. The assessee also prayed for relief in respect of surcharge and education cess paid by mistake.

4. However, the CIT rejected the above contentions and observed that no amount was payable by the assessee in terms of the intimation under Section 143(1) of the Act and therefore no prejudice was caused to the assessee in terms thereof. He also observed that if the assessee was of the view that its income was chargeable to tax at 10% it should have mentioned the same in its return of income or should have subsequently filed revised return. It was held that Section 264 of the Act could not be invoked to rectify the assessee's mistake, if any.

5. **The assessee filed a writ petition against the order of the CIT rejecting the petition filed u/s. 264.**

Held

1. The Court observed that in *Vijay Gupta vs. CIT* (2016) 68 taxman.com 131 (Del) it was held that "intimation under section 143(1) is regarded as an order of the purposes of section 264 of the Act".

2. The assessee had voluntarily paid tax at the rate of 20% in terms of the Indo-Spain DTAA as tax on FTS and therefore there was no further tax to be paid at the time of filing of the return. However, it was not even denied by the Department that the assessee committed a mistake and should have paid tax at 10%. Even though, this extra 10% was paid by the assessee was of its own volition, it was indeed prejudicial to the assessee. Consequently, all the ingredients of Section 264 of the Act got attracted.

3. Thus, the Court quashed the order passed by the CIT and directed the Respondents to permit the assessee to rectify its return by paying tax on FTS at 10%.

2 *PCIT vs. Sterling Oil Resources Ltd.*

[TS-639-HC-2019(BOM)] - ITA 341 of 2017

Share application money paid to an AE which remained with it for a considerable period of time could not be recharacterised as loan in absence of any material on record to suggest that the transaction was a sham. Consequently, no notional interest could be taxed in respect of the said share application money

Facts

1. The assessee-company had applied for allotment of shares of its AE. Such shares were, eventually allotted but after a gap of more than two years. The Department held a belief that for the period during which the share application money remained parked with AE, the same should be brought to tax on notional interest basis.

2. The Tribunal deleted the addition on the ground that the Assessing Officer cannot recharacterise the transaction. Thus, it was held that in the present case there was no interest free loan by the assessee to its AE

3. Aggrieved, the Revenue filed an appeal before the High Court.

Held

1. The Court had under similar circumstances dismissed Revenue's Income Tax Appeal No. 1248/2016 holding that TPO could not disregard the apparent transaction and substitute the same without any material of exceptional circumstances pointing out that the assessee had tried to conceal the real transaction. It observed that TPO could not question the commercial expediency of the assessee entering into such transaction.

2. Accordingly, it dismissed Revenue's appeal as no substantial question of law arose.

3 *PCIT vs. Li and Fung (India) Pvt. Ltd.*

[TS-658-HC-2019(Del)] – ITA NO. 176 of 2019

An entity that is a captive service provider cannot be compared to an entity providing service to large number of outside entities

Facts

1. The assessee, a captive unit and subsidiary of Li & Fung (South Asia Limited), a Company incorporated in Mauritius was engaged in the business of providing sourcing support services for which it was paid service charges at cost plus mark-up of 8%.

2. The PLI of the assessee company was computed by the assessee at 7.92% whereas the average PLI of the comparables was computed at 3.76% as per the analysis in the transfer pricing document. On reference being made to TPO a new search process was conducted with the final list having seven comparables and the PLI was

computed at 14.35%. The TPO had also included Axis Integrated System Ltd. as comparable noting that as per the annual report the said company had received income under the Head of "liaisoning charges" which as per the TPO showed that the said company was also providing business support services, similar to assessee's function.

3. The DRP upheld the TPO's order.

4. In appeal by assessee, the Tribunal excluded the said comparable.

5. Aggrieved, the Revenue filed an appeal before the High Court.

Held

1. The Court noted that the Tribunal had rightly pointed out that no comparison could be drawn between an entity that is a captive service provider to its group entities and an entity like Axis, which was providing liaisoning services to a large number of entities. More importantly, Axis was also engaged in the business of issuing digital certification.

2. The Court also relied on its earlier decision in the case of *Rampgreen Solutions Pvt. Ltd. vs. CIT* 377 ITR 533 (Del) wherein it was held that *"comparability analysis by the transactional net margin method may be less sensitive to certain dissimilarities between the tested party and the comparables. However, that cannot be the consideration for diluting the standards of selecting comparable transactions/entities. A higher product and functional similarity would strengthen the efficacy of the method in ascertaining a reliable arm's length price. Therefore, as far as possible, the comparables must be selected keeping in view the comparability factors as specified. Wide deviations in profit level indicator must trigger further investigations/ analysis."*

3. Accordingly, the appeal filed by the Revenue was dismissed.

4 ***Pr. CIT vs. BirlaSoft (India) Pvt. Ltd.***
[TS-672-HC-2019 (Delhi)] - ITA No. 587 and 596 of 2019

Where assessee was a service provider to its associated enterprise (AE) as well as non-AEs internal benchmarking analysis could be done for determining arm's length price

Facts

1. The assessee-company had adopted Internal TNMM method for benchmarking of International transactions for provision of software development services for AY 2012-13 and 2013-14

2. The TPO/AO rejected the adoption of the said method.

3. The Tribunal allowed assessee's appeal following its order in assessee's own case for the assessment year 2008-09 wherein it was held that

i. The assessee was justified in undertaking internal benchmarking analysis on standalone basis by placing on record working of operating profit margin from international transactions with AEs and transactions with unrelated parties undertaken in similar functional and economic scenario, and the same should be the basis for determination of arms's length price in respect of international transactions undertaken with the associated enterprise

ii. The TPO had no mandate to have recourse to external comparables when in the present case, internal comparables were available, which could be applied for determining the arm's length price of international transactions with AEs.

4. Further, the Tribunal also noted that the aforesaid decision of the Tribunal for AY 2008-09 was also followed by the Tribunal in AY 2009-10 which was upheld by Hon'ble Delhi High Court in ITA No. 44/2015.

5. Aggrieved, Revenue filed an appeal before the High court.

Held

1. The Court noted that Hon'ble Delhi High Court in ITA No. 44/2015 in assessee's own case in AY 2009-10 had held that since the assessee was a service provider to its associated enterprise (AE) as well as other foreign customers or non-AEs, the suggestion that the non-AE transactions which reported lower margins are to be used for benchmarking the AE transactions was acceptable. Thus, no adjustment was called for. Furthermore, the Tribunal's reasoning was in accord with Rule 10B(1)(e)(ii) of the Income-tax Rules.

2. Accordingly, the appeal filed by the Revenue was dismissed.

5 ***Cognizant (Mauritius) Ltd. and Anr. vs. Deputy Commissioner of Income-tax, (International Taxation)***

[2019] 106 taxmann.com 389 (Madras) -W.P. Nos. 1244 & 1245 OF 2018

When an order is passed by AO which is not in conformity with report submitted by TPO, the assessee can file objections before DRP against the said order and writ petition for the same is not maintainable

Facts

1. The Petitioners were the shareholders in Cognizant Technology Solutions India Private Limited [In short "CTSIPL"]. As on 31-3-2013, one of the Petitioners i.e., Cognizant (Mauritius) Limited owned 1,39,93,649 shares and the other Petitioner Cognizant Technology Solutions Corporation, USA owned 39,60,000 shares in CTSIPL.

2. The Board of Directors of CTSIPL resolved that the shares could be bought by CTSIPL at the value of ₹ 23,915/- per share under Section 77 A of the Companies Act. CTSIPL had ascertained valuation of its shares through SEBI registered Category-I Merchant Banker and the price per share of the Company, based on the valuation undertaken using the Discounted Free Cash Flow ["DCF"] method, was ₹ 23,915.10.

3. The AO referred the determination of ALP for buy-back of shares to the TPO. TPO passed an order on 31-10-2017 accepting the transaction to be at ALP. Thereafter, a show cause notice was served by the AO on the Petitioners and a draft Assessment Order was passed on 31-12-2017 contending that FMV of the aforesaid shares was ₹ 8,512/- and consequently the excess consideration over the said FMV was assessed under Section 56(1).

4. The Petitioners filed a Writ Petition contending that the draft order was passed in violation of the principles of natural justice and in contravention of Section 92CA(4) of the Act, and since AO had failed to pass draft assessment order in conformity with TPO's order, the Dispute Resolution Panel had no jurisdiction to consider the objection of the Petitioners.

5. The Respondents filed a Counter Affidavit contending that the Writ Petition was liable to be dismissed *in limini* as the Petitioners had an effective and efficacious alternative remedy under the IT Act. They were entitled to file objections before the DRP under Section 144-C of the IT Act or to file an appeal against the final assessment order before the Commissioner of Income Tax (Appeals) under Section 246A of the IT Act.

Held

1. The Court framed the following questions for consideration :-

(i) whether principles of natural justice had been violated as alleged by the petitioners and

(ii) whether these Writ Petitions were maintainable at this stage.

2. The Court noted the fact that the Authorized Representative of the Petitioner-Company had appeared before the Respondent and submitted the documents and a reply to the show cause notice. Thus, there was no breach of principles of natural justice.

3. The Court further held that a plain reading of the sub-section (6) of Section 144 C of the IT Act made it clear that the Dispute Resolution Panel had very wide powers to consider all the materials and pass appropriate orders under 144C(7) of the Act. Thus, the Writ Petition was dismissed and Petitioners were given the liberty to raise all the issues before the Dispute Resolution Panel within two weeks from the date on which the judgment/order was made ready.

B. Tribunal Decisions

6 ***Kingfisher Airlines Ltd vs. DDIT***
[TS-430-ITAT-2019(Bang.)]

Payment made to Non-Resident for using foreign training facilities (in Dubai, Germany and Singapore) for training its pilots and cockpit crews out-side India cannot be regarded royalty/FTS

Assessment years : 2007-08 & 2008-09

Facts

i) The assessee (Kingfisher Airlines Ltd.) made payments to non-residents for training pilots and cockpit crew to Dubai, Germany and Singapore respectively. The training facilities were all located outside India, the training was given in the said countries and payments for the same were also made outside India. Thus, all ingredients of the transaction were outside India. It was claimed that the training given by the above companies was part of their routine business, involved use of technology by the training companies however did not involve transfer of any technology to employees of assessee.

ii) The assessee thus did not treat these services as fees for technical services (FTS). AO, on the other hand treated assessee as defaulter as per provisions of section 201(1) and 201(1A) for having not deducted tax at source u/s. 195 in respect of the payments made as aforesaid to non-residents. AO opined that these payments had the character of FTS u/s. 9(1) (vii) as well as relevant DTAA between India and the respective countries of which the recipients of payment from the Assessee were tax residents.

iii) CIT(A) held that payment made to Lufthansa Germany was not Royalty and payments made to UAE concern was not liable for tax in India and accordingly provisions of Section 195 were not applicable. With respect to payments made to Singapore, CIT(A) directed to reduce simulator usage fees from total payments and treat the balance amount as FTS liable for tax deduction u/s. 195 and directed the AO to recompute tax payable u/s. 201(1) and interest u/s. 201(1A).

iv) Aggrieved, both assessee and Revenue filed an appeal with Bangalore ITAT.

Decision

The Tribunal held in favour of the assessee as under:

i) ***Re: Payment made to M/s. Lufthansa, Germany***

ITAT noted that a flight simulator was an essential part of training imparted to the pilots and crew of aircraft and the hourly quantification of such charges for use of the simulator did not mean that the assessee was hiring the same or making payment for a right to use the same. ITAT held that without the imparting of training by the instructors, the hiring of simulator on its own did not have any purpose and hence it could not be said that the assessee paid royalty for use of simulator;

ii) Payment to M/s. CAE Aviation, Dubai

ITAT held that this payment was not in the nature of Royalty. ITAT observed that the question whether it was FTS did not arise because of the absence of a clause relating to FTS in the DTAA regarding FTS and the settled position of law that in the absence of a clause in a treaty not dealing with a particular item of income, the same should not be regarded as residuary income but income from business and in the absence of Permanent Establishment in India (PE) of the non-resident in India, the same cannot be taxed. ITAT found that CIT(A)'s decision was in line with Co-ordinate Bench ruling in case of ABB FZ-LLC [TS-8702-ITAT-2017 (Bangalore)-O], which was a case rendered in the context of DTAA between India and UAE. ITAT held that CIT(A)'s decision was a correct interpretation of the treaty and found no grounds to interfere with the decision of the CIT(A) on this issue.

iii) Payments made to M/s. Alteon Singapore

(a) ITAT found that CIT(A) had upheld AO's order only on the ground of insertion of an explanation for retrospective amendment to the Sec. 9 by (by the Finance Act, 2010) from 1-6-1976. ITAT stated that, *"tax deduction at source obligation cannot be fastened on a person on the basis of a retrospective amendment to the law, which was not in force when the payments were made."* ITAT observed that Revenue sought to rely upon the *Explanation 2* to section 195 inserted by Finance Act of 2002 w.r.e.f 1-4-1961 which laid down that even if the payment by a resident in India to a non-resident constitutes business income in the hands of the non-resident then irrespective of the existence or non-existence of a permanent establishment of the non-resident in India, tax is liable to the deducted at source by the resident in India making payment to non-resident. ITAT noticed that such provision did not exist at the time when the assessee made such payments to the non-resident and it was not possible for the assessee to foresee an obligation to deduct tax at source by a retrospective amendment to the law. ITAT opined that amendment brought in by the Finance Act with retrospective effect, which was passed in the year subsequent to the year under consideration, should not be considered for penalizing the assessee by treating him as an assessee in default.

(b) Relying on *Kerala Vision Ltd.* [TS-342-ITAT-2014(COCH)-O], TTK Prestige Ltd [TS-6739-ITAT-2014 (Bangalore)-O] and *Asia Satellite Telecommunications Co. Ltd.* [TS-823-HC-2011(DEL)-O] ITAT held that a liability to deduct tax at source cannot be fastened on an assessee on the basis of a retrospective amendment to the law.

(c) ITAT concluded that CIT(A) erred in holding that FTS was taxable in India only because of the retrospective amendment to the law and he erred in not holding that the liability to deduct tax at source arises at the time of making payment and therefore there would be no obligation to deduct tax at source. Accordingly, the order of the CIT(A) holding assessee to be an assessee in default u/s 201(1) of the Act to the extent of the payment relating to FTS and consequent liability towards interest u/s. 201(1A) of the Act was cancelled by ITAT allowing assessee's appeal.

7 ***DCIT vs. Sri K. E. Faizal***
[TS-389-ITAT-2019(COCH)]

India-UAE DTAA – Short Term Capital Gains arising to a Non-Resident on sale of units of equity oriented mutual funds are not taxable under India-UAE treaty

Assessment Year: 2012-13

Facts

i) The assessee, a Non-Resident in India for the Assessment Year (AY) 2012-13, was a resident of the UAE and had obtained a Tax Residency Certificate from the revenue authorities of the UAE for the relevant period.

ii) During the AY 2012-13, the assessee had sold equity oriented mutual funds in India and had STCG from such sale amounting to INR 13,499,407.

iii) While filing the India tax return for the said AY, the assessee had claimed such STCG as exempt by virtue of Article 13(5) of the Treaty.

iv) During the scrutiny assessment, the Assessing officer (AO) had held that the underlying instrument of an equity oriented mutual fund is a share and consequently, as per Article 13(4) of the Treaty, STCG should be taxable in India. Accordingly, the AO denied such exemption claimed by the assessee and added a sum of INR 13,499,407.

v) Aggrieved by the order passed by the AO, the assessee had filed an appeal with the Commissioner of Income-tax (Appeals) CIT(A). The CIT(A) relying on *ITO (IT) vs. Satish Beharilal Raheja* [(2013) 37 taxmann.com 296 (Mumbai-Trib.] held that STCG would not be taxable in India as the equity oriented mutual funds are not shares and therefore Article 13(5) of the Treaty (and not Article 13(4)) would be applicable.

vi) Aggrieved by the order of the CIT(A), the tax department had filed an appeal with the Tribunal.

Decision

The Tribunal held in favour of the assessee as follows:

i) Before the Tribunal, the tax department contended that the underlying instrument of any equity oriented mutual fund is nothing but a share and hence the gains arising from the sale of equity oriented mutual fund would result in sale of shares. Accordingly, such gains from sale of shares (units of mutual funds in the instant case) is taxable under Article 13(4) of the Treaty which provides that income arising to a resident of UAE from transfer of shares (and not any other property) in India, may be taxed in India.

ii) Tribunal observed that the assessee had qualified to be a NR and accordingly, the sale of equity oriented mutual fund in India would be taxable in India u/s. 5(2) of the Income-tax Act, 1961.

iii) However, considering the provisions of the treaty, the Tribunal observed the following:

(a) Term, 'share' is not defined under the treaty; hence share would carry the meaning as per the Act.

(b) As per the provisions of Securities and Exchange Board of India (Mutual Funds) Regulations, 1995, mutual funds in India can be established only in the form of 'trusts' and 'not companies'.

(c) The definition of Security under the Securities Contract (Regulation) Act, 1956, it can be inferred that shares and units of mutual funds are two different types of securities.

(d) As per Article 13(5) of the Treaty, income arising to a resident of UAE from transfer of property other than shares in an Indian company, are liable to tax only in the UAE. The Tribunal also placed reliance of *ITO (IT) vs. Satish Beharilal Raheja* [(2013) 37 taxmann.com 296 (Mumbai-Trib)] and *Apollo Tyres Ltd vs. CIT* [2002J 122 Taxman 562 (SC) wherein it was held that units of mutual funds cannot be regarded as shares.

iv) Given the above, the Tribunal held that for an assessee who is a resident of UAE, STCG arising from sale of units of mutual funds (and not shares) are not liable to tax in India and consequently dismissed the appeal of the tax department.

8 *Linklaters LLP vs. DCIT*

[2019-TII-172-ITAT- Mum-INTL]

India-UK DTAA – Determination of Service PE - To determine a threshold for Service PE under the India-UK tax treaty 'any 12 month period' is to be construed as previous/ financial year

Assessment Year : 2002-03

Facts

i) The assessee, a Limited Liability Partnership, is a tax resident of U.K. and it offers legal consultancy services to its clients all over the world including India. During the Assessment Year (AY) 2013-14, the assessee provided professional services to its Indian clients.

ii) The assessee contended that it did not have PE in India in terms of Article 5(2)(k)(i) of the tax treaty as its employees did not stay in India more than 90 days during the relevant year. The expression 'any twelve month period' as used in Article-5(2)(k)(i) of the tax treaty has to be construed as previous year relevant to AY under consideration. The aforesaid ratio has been laid down by the Tribunal in *Linklaters LLP vs. DCIT* [2018-TII-348-ITAT-MUM-INTL] while deciding its own case. The assessee contended that the total number of days spent by the employees in India was 42 days. Therefore, in terms of Article-5(2)(k)(i) of the tax treaty, the assessee did not have PE in India during the year.

iii) The tax department contended that the expression 'any twelve month period' as used in Article-5(2)(k)(i) of the tax treaty would not mean the previous year as defined in Section 3 of the Act. The tax department contended that, had it been the case, then, like Article-5(2)(k)(i) of the tax treaty, fiscal year which has been defined to be the previous year would have been used in Article 5(2)(k)(i) of the tax treaty. Thus, the meaning ascribed to fiscal year cannot be ascribed to the term 'any twelve months period'.

Decision

The Tribunal held in favour of the assessee as follows:

i) The Tribunal relied on assessee's own case for the AY 2012-13. The Tribunal in earlier case observed that the AO referring to Article 5(2)(k)(i) of the tax treaty had concluded that the assessee had a PE in India, since, its employees or personnel have rendered services in India for a period of 90 days or more within any 12 month period. However, the Tribunal observed that the expression 'any 12 month period' as used in Article 5(2)(k)(i) of the tax treaty had not been defined anywhere in the tax treaty.

ii) Therefore, the meaning of the said expression could be taken with the aid of the provisions of the Act, since, the income is sought to be taxed in India. Section 5 of the Act which defines scope of total income refers to the total income of any previous year of a person who is a resident. Similarly, Section 6 of the Act postulates that an individual or a HUF or a company or any other person can be considered to be a resident in India in any previous year if it satisfies the condition mentioned therein.

iii) Thus, for the purpose of being considered as a resident in India a reference had been made to the previous year. Section 4 of the Act, which is the charging section, mandates that a person shall be charged to income tax in respect of the total income of the previous year. The expression 'previous year' has been defined under Section 3 of the Act to mean the financial year immediately preceding the AY. Thus, as per the provisions of the Act, the 12 month period would mean the previous year or the financial year which is the unit for which the income of a person is taxable.

iv) If the provisions of Article 5(2)(k)(i) of the tax treaty is read harmoniously with the provisions of the Act, it would be fair and reasonable to conclude that the expression 'any 12 month period' mentioned in Article 5(2)(k)(i) of the tax treaty had to be construed to mean the previous year or financial year as per Section 3 of the Act, since, the income is sought to be taxed in India.

v) Therefore, the Mumbai Tribunal in the instant case directed the AO to verify as to whether the employees/personnel of the assessee were situated in India for rendering services for a period not exceeding ninety days during the previous year and if it is found to be so, then, it has to be held that the assessee did not have a PE in India during the year under consideration.

❍❑❍

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INDIRECT TAXES

CA Rajkamal Shah, CA Vikesh Doshi & CA Sudarshan Gaykar

GST Gyan – Exempt Supply and ITC Reversal under GST

The assessee is always at loggerheads with the tax department when it comes to allowance of input tax credit, may it be excise duty or service tax or VAT or now GST. As a principle of Value Added Tax, it is accepted that a manufacturer, trader or service provider should get seamless credit of the duties or taxes paid on their inputs, the government or the tax department always tries to see that somehow the credit is restricted/disallowed.

The issue of disallowance of Input Tax Credit in India is an age-old issue right from MODVAT days. In olden excise days, such attempts were foiled when the highest court of the land pronounced its judgment in *Eicher Motors Ltd. in 1999 (106) E.L.T. 3 (SC)* and the decision was followed in most of the cases, prominent amongst them is *Dai Ichhi Karkaria Ltd. [1999 (112) E.L.T. 353 (SC)]*. It is thus a settled position in law that the eligibility to ITC is required to be ascertained on the basis of statutory provisions as existing on the date of claim. Once the taxpayer finds himself within the four corners of statutory provisions to claim the ITC, his right to ITC becomes absolute and the credit so taken becomes indefeasible. The Supreme Court has ruled that such credit was "as good as tax paid".

Be as it may, the basic rationale for reversal of input tax credit is that any procurements are used for exempted supplies, either commonly or exclusively, such credit cannot be claimed since output tax on such outward supplies is not payable except for zero rated supplies (export outside India and SEZ supplies).

This article intends to throw light on input tax credit reversals in respect of inputs and input services to be made on account of exempt supplies undertaken by tax payer considering the Act and rules, when they were introduced and as per the amendment made therein in 2019.

Let us now examine the issue of reversal of credit in relation to exempt supply under the GST law. Section 16 of the CGST Act, 2017 deals with the allowability of input tax charged on any supply of goods or services or both to him which are used or intended to be used in the course or in furtherance of his business and the said amount shall be credited to the Electronic Credit Ledger (ECL) of such person subject to certain conditions and restrictions.

However, it must be noted that the entitlement of ITC is very widely conferred on the taxpayer. At the cost of repetition, we will summarise this as follows:

- Input Tax Credit should be used in the course of business or in furtherance of the business.

- Input Tax Credit can also be availed if the same is intended to be used in the course of business or in furtherance of the business.

The conditions of availment of credit are prescribed u/s. 17 which can be summarised as follows:

- To disallow the credit that are used partly for business purpose and partly for other purpose (we would call it credit in relation to 'common supplies'). The term, 'other purpose' is not defined. One instance of 'other purpose' can be personal use of the taxpayer.

- From the credit used for business purpose, the ITC used partly for effecting taxable supplies including zero rated supplies (both under CGST Act & IGST Act) and partly for exempt supplies is to be carved out. The formula of restriction of ITC in relation to supply of goods or services or both to former kind of supplies is prescribed under R. 42 of CGST Rules, 2017 by virtue of sub-section (3).

  The formula for restriction of ITC in relation to capital goods is prescribed in Rule 43. However, restriction in relation to capital goods is not subject matter of this article.

  i) For the purpose of this sub-section, the exempt supply would include the supplies on which the recipient is liable to pay tax on reverse charge basis

  ii) Transaction in securities (1% of value of sale of securities to be taken as valuation for the purpose of reversal)

  iii) Sale of buildings or part thereof, other than that covered under clause 5(b) of Sch. II, i.e. sale of completed building or part thereof after issue of Completion Certificate for which no consideration is received prior to such completion (for brevity's sake we will call it 'unsold flats'). (the value of completed flats shall be as adopted for the purpose of stamp duty)

  iv) Sale of land (the value as adopted for the purpose of stamp duty)

  v) An *Explanation* is inserted to sub-section (3) effective from 1st February 2019 to exclude all the items prescribed under Sch. III, except in case of completed flats and sale of land. However, the *Explanation* appears to be only clarificatory as otherwise such legislative intent was already indicated *vide* sub-section (3) by including only sale of land and unsold flats for the purpose of computation of exempt supplies.

Rule 42 of CGST Rules as originally promulgated prescribed the formula to arrive at the reversal of input tax credit in relation to exempt supplies. Such reversal of input tax credit is required to be made tax period wise. The 'tax period' is defined as the period for which the return u/s. 39 is required to be filed. However, at the end of the financial year, the assessee is finally required to compute the eligible input tax credit and reverse or claim excess availed or short availed ITC respectively before due date for filing return of September following the end of financial year, to which such credit is claimed.

In case of excess availment of ITC during the financial year, the difference is required to be paid with interest of 18% to be computed from 1st April of the subsequent financial year till date of reversal (last date for such reversal is due date for filing return of September following the end of relevant financial year). Similarly, in case of shortfall of claim of ITC, such difference can be availed till the said date.

The determination mechanism prescribed in Rule 42 of CGST Rules 2017 is tabulated below for the sake of clarity. This Rule is applicable to all kinds of tax payers prior to the amendments:

Tax period wise manner of determination of ITC in respect of inputs and input services in relation to common supplies. **Total ITC ₹ 100,000/-, Exempted Turnover ₹ 3,00,000 (denoted as 'E') and Total Turnover ₹ 10,00,000 (denoted as 'F')**			
	Particulars	***Amt. (ITC) ₹***	***Denotation***
Total Input tax credit in a tax period		100,000/-	T
Less:	Amount of ITC exclusively used or intended to be used for the purposes other than business	10,000/-	T1
Less:	Amount of ITC exclusively used or intended to be used for exempt supplies	20,000/-	T2
Less:	Blocked credit as per S. 17(5)	5,000/-	T3
	Amount of ITC to be credited to ECL (Electronic credit ledger)	65,000/-	C1 = (T - {T1 + T2 + T3})
Less:	ITC directly attributable to taxable (incl. zero rated supply)	50,000/-	T4
	Common credit	15,000/-	C2 = (C1 - T4)
	Amount of ITC attributable towards exempt supplies	4,500/-	D1 = (E/F *C2) say ₹ 3 lakhs/ 10 Lakhs = 30%
	Credit attributable to non-business purposes used partly for business and partly for non-business	750/-	D2 = C2*5%
	Eligible Common Credit	9,750/-	C3 = (C2 - {D1 + D2})
The amount of C3 shall be computed for CGST, SGST, UTGST & IGST separately for each tax period. ITC required to be reversed = D1 + D2 = ₹ 5,250/-			

Note :

- **The reversal is based on the value of supply.**
- The amount of D1, D2 is to be added to output liability of each tax period. However, now, such amounts are to be either reversed in GSTR-3B or paid through DRC-03 (either in cash or credit).
- Registered person who does not have any turnover during the said period turnover of last tax period shall be considered for computing the exempt turnover.
- The amount determined under sub-rule (1) shall be calculated finally for the financial year before the due date for furnishing of the return for the month of September following the end of the financial year to

which such credit relates, in the manner specified in the said sub-rule (2).

The aforesaid value-based formula prescribed under Rule 42 of CGST Act 2017 is common for all tax payers up to 1-4-2019. However, with the amendment effective from 1-4-2019, a separate methodology of reversal is carved out for the builders and developers, who have inventory of unsold flats as on the date of Occupancy Certificate or first occupation, whichever is earlier.

Impact of amendments in sub-rule (1), (2) and insertion of sub-rules (3), (4), (5) and (6) to Rule 42 to alter the methodology to compute reversal of input tax credit in relation to unsold flats

- T4 shall be considered zero in respect of any tax period which means all credit shall be regarded as common credit on which proportionate reversal shall apply.
- Such reversal of credit shall be calculated for each project separately based on area being constructed.
- Instead of reversal of input tax credit, relating to unsold flats on date of OC, in the tax period having sale of such unsold flats, now it is required that the reversal of accumulated input tax credit including the transitional credit in the proportion of the area of the unsold flats to the total area at the time of issue of Completion Certificate or first occupation, whichever is earlier.
- The builders/developers shall be required to reverse the accumulated input tax credit including the transitional credit as on 1-7-2017 in relation to unsold flats finally at the time of issue of OC to compute the eligible input tax credit. In case of excess availment of ITC, the difference is required to be paid with interest of 18% from 1st April of the subsequent financial year but before the due date for filing the return for the month of September following the end of financial year to which such credit relates. Similarly, in case of shortfall of claim of ITC, such difference can be re-credited at the time of issue of Occupation Certificate or first occupation, whichever is earlier.

Manner of determination of reversal of ITC in respect of inputs and input services after 1-4-2019 for builders and developers. Assumptions: Total carpet area 70,000/- sq. ft. and total unsold area, as on date of OC or first occupation, whichever is earlier, 50,000/- sq. ft. area.			
Particulars		***Amt. (ITC) ₹***	***Denoted as***
Total Input tax credit in a tax period		100,000/-	T
Less:	Amount of ITC exclusively used or intended to be used for the purposes other than business	10,000/-	T1
Less:	Amount of ITC exclusively used or intended to be used for exempt supplies	20,000/-	T2
Less:	Blocked credit as per S.17(5)	5,000/-	T3
	Amount of ITC to be credited to ECL	65,000/-	C1 = (T - {T1 + T2 + T3)
Less:	ITC attributable to taxable supply (one to one) (incl. zero rated supply)	0/-	T4 (See Note 1)
	Common credit	65,000/-	C2 = (C1 - T4)

Particulars		*Amt. (ITC) ₹*	*Denoted as*
	Amount of ITC attributable towards exempt supplies	46,429/-	D1 = (E/F) * C) (Note 2)
	Credit attributable to non-business purposes used partly for business and partly for non-business	3,250/-	D2 = C2*5% (Note 3)
	Eligible Common Credit	15,321/-	C3 = (C2 - {D1 + D2}) (Note 3)
The amount of C3 shall be computed for CGST, SGST, UGST & IGST separately for each tax period. ITC required to be reversed= D1 + D2 = ₹ 49,679/-			

Note 1

Explanation has been inserted from 1-4-2019 to prescribe the quantum of ITC directly related to taxable supplies to be 'zero' for the purpose of computation of reversal.

Note 2

The value of 'E/F' for a tax period shall be calculated for each project separately, taking value of E and F as under:

Denoted as	*Particulars*	*Area considered in above e.g.*
E	Aggregate carpet area of the apartments, construction of which is exempt from tax plus aggregate carpet area of the apartments, construction of which is not exempt from tax, but are identified by the promoter to be sold after issue of completion certificate or first occupation, whichever is earlier	50,000/- sq. ft.
F	Aggregate carpet area of the apartments in the project	70,000/- sq. ft.

Note 3

We have assumed that common ITC is commonly used for undertaking business activities as well as non-business activities (such as personal use). Hence, 5% of such common credit is to be reversed.

Impact of insertion of sub-rule (4) to Rule 42 for other than RREPs, which have migrated to new tax rates from 1st April, 2019

In case of residential real estate projects (REP) transitioned to new tax regime from 1st April 2019, reversal of inputs and input services commencing on 1-7-2017 to 31-3-2019 in each project is to be computed finally for commercial portion (area wise). The reversal is to be made in respect of the carpet area of unsold flats to the aggregate carpet area of commercial apartments before the due date of furnishing the return for the month of September following the financial year in which the completion certificate is issued or first occupation takes place. Interest @18% is required to be paid In case of excess availment of ITC till date of reversal. Similarly, in case of shortfall of claim of ITC, such difference can be availed till the said date.

The reversal is to be made in the following manner:

C3 final common = C3 aggregate common x (E/F).

The denotations are explained below.

– C3 aggregate common credit = sum of ITC derived in below explained manner:

1. Aggregate amount of C3 as determined under sub-rule (1) to Rule 42 during period starting 1st July, 2017 or date of commencement of project, whichever is later, till 31 March, 2019 x AC/AT

   AC = total carpet area of the commercial apartments in the project

   AT = total carpet area of all apartments in the project

   By virtue of this formula, credit pertaining to commercial portion of project is being carved out from total credit claimed till March 2019 including transition credit.

+

2. Aggregate amount of C3 determined under sub-rule (1) for the period starting 1st April, 2019 till date of completion or first occupation, whichever is earlier.

– E = total carpet area of commercial apartments which have not been booked till the date of issuance of completion certificate or first occupation of the project, whichever is earlier.

– F = total carpet area of the commercial apartments in the project

Manner of determination of reversal of ITC in respect of inputs and input services for REP builders and developers, who have transitioned to new tax regime.

Assumptions: Total carpet area 70,000/- sq. ft., total commercial area 20,000/- sq. ft. and total unsold area, as on date of completion certificate i.e., July 2019, 15,000/- sq. ft. area including 5,000/- sq. ft. of commercial area. The aggregate amount of C3 determined under sub-rule (1) ₹ 50,000/- and aggregate amount of C3 for period starting April 2019 till the date of completion certificate ₹ 20,000/-

	Particulars	***Amt.(ITC) ₹***	***Denoted as***
	Aggregate Common Credit (C3 as per sub-rule (1) of Rule 42) from 01-7-2017 to 31-3-2019	50,000/-	C3
	Credit attributable to commercial area in project	14,285/-	Aggregate comm C3 (A) = C3 * AC/AT (₹ 50,000* 20,000 sq. ft./70,000 sq. ft.)
Add:	Aggregate amount of C3 from 1st April, 2019 to date of completion or first occupancy, whichever is earlier	20,000/-	Aggregate comm C3 (B)
	Aggregate common credit attributed to commercial area	34,285/-	Aggregate Common Credit C3 = A + B above

	Particulars	Amt.(ITC) ₹	Denoted as
	Aggregate common credit attributed to exempt supplies – unsold commercial area as on date of OC (July 2019)	8,706/-	C3 final common * E/F (₹ 34,285/- * 5000 sq. ft. (unsold commercial area on date of OC)/20,000 sq. ft. (total commercial area of project)
The above C3 final common credit has been computed for July 2019 (in which, OC is received) in respect of REP, which has transitioned to new tax regime. The amount of eligible credit ₹ **25,579/-.**			

For RREP migrated to new tax rate regimen no reversal required in Rule 42

As per sub-rule (5), in case of RREP who have migrated to new tax regime, final reversal as on date of OC or first occupation is not required to be undertaken since the reversal of credit claimed till 31st March, 2019 is already made on or before 30th September, 2019 *vide* Annexure II to Notification No. 3/2019-CGST.

With regard to period starting 1st April, 2019 for such projects, ITC is not allowed to claim any credit.

Credit in respect of common inputs and input service used for more than one project

In terms of newly inserted sub-rule (6) to Rule 42, the builder/developer shall assign such credit on a reasonable basis and reversal shall be made for each project in accordance with sub-rule (3) of Rule 42.

Conclusion

Rule 42 as originally promulgated took care to reverse the input tax credit in relation to inputs and input services in relation to exempt supplies in accordance with S. 17(1), (2) and (3) read with sub-section (6) of the CGST Act in general. Sub-section (3) of Section 17 targeted even the reverse charge basis payments in respect of which the tax is payable by the recipient. Further amendments were made in Rule 42 w.e.f. 1-4-2019 to give to target the builders/developers specifically and to give effect to the new rate of tax on real estate regime introduced by Notification 3/2019-CT (Rate). It does raise the question that the builders/developers who were not fitting into the unamended Rule 42 at all required to reverse the credit in respect of unsold flats as on the date of issue of completion certificate or the first occupation, whichever is earlier on account of lack of proper mechanism and the legal battle may go on. All said and done, the amendments from 1-4-2019 are very meticulously made and removed the lacuna of reversal of input tax credit in relation to exempt service on unsold flats. Attempt has been made to explain the formulas of different situations in the tables above lucidly.

Though not in conformity with the Supreme Court rulings discussed above for which the battle can go on, now it is provided in no unequivocal terms that such reversal shall be made even for the transition credit taken on 1-7-2017 for the then ongoing projects which may not have force of the existing laws subsumed under GST. Further, logically the reversal is required to be made on the proportion of carpet area of the unsold flats to the aggregate carpet area, project wise, instead of value based reversal which was not practically and fundamentally possible. Also the reversal will now have to be made finally by the due date of filing of return of September for the previous financial year in which completion certificate is issued or first occupation has taken place, however the issue of tax period wise reversal still looms large as hanging sword on the head of the builders/developers.

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GST – Recent Judgments and Advance Rulings

A. Writ Petitions

1. AAP AND COMPANY (2019-TIOL-1422-HC-AHM-GST)

Facts, Issue involved and Contention of Petitioner

Petitioner is a practicing Chartered Accountant registered under GST. Writ application was filed in the Gujarat High Court seeking the validity and legality of press pelease dated 18th October, 2018 to the extent of its para 3.

As per the press release dated 18th October, 2018, the last date for claiming Input Tax Credit (ITC) for the period July 2017 to March 2018 is the date for filing the return in Form GSTR-3B for the month of September. Thus, a taxpayer will not be able to claim ITC for the period July 2017 to March, 2018 after the last date of filing of Form GSTR-3B for the month of September.

This disentitles a taxpayer to claim ITC for said period, which could not be taken because of any error or commission.

Petitioner's submissions

Section 16(4) of the CGST Act, 2017 provides *that a registered person shall not be entitled to claim ITC in respect of any invoice or debit note for supply of goods or services or both after the due date of furnishing of the return under Section 39 for the month of September following the end of the financial year to which such invoice or invoice relating to such debit note pertains or furnishing of the relevant annual return, **whichever is earlier***.

Section 39(1) of the CGST Act/GGST Act provides that every registered person shall furnish a monthly return in such form and manner as may be prescribed. The form and the manner of submission of monthly return is provided in Rule 61 of the CGST/GGST Rules. Bare perusal of Rule 61 of the CGST/GGST rules indicates that the return prescribed in terms of Section 39 is a return required to be furnished in Form GSTR-3 and not GSTR-3B.

From a conjoint reading of Rule 61(1) and Rule 61(5) of the CGST/GGST Rules and Notification No. 17/2017-Central Tax dated 27-7-2017 that the return required to be furnished in Form GSTR-3B is not the return in lieu of a return specified in Form GSTR-3.

Rule 61(6)(c) of the CGST/GGST Rule provides that if any input tax credit is taken after filing of the GSTR-3B return and it is reflected in return filed in Form GSTR-3 then the same will have to be credited to the electronic credit ledger of the registered person.

Applicant further submitted that the decision to add return in Form GSTR-3B was taken in the 18th GST Council held on 30th June 2017 on account of the reason stated as 'shorter return for first two months of roll out'. It has not been introduced as a return in substitute of return to be filed in Form GSTR-3. Therefore, return in Form GSTR-3B is only a temporary stop gap arrangement till due date of filing return in Form GSTR-3 is notified in the GSTN portal. It is obvious that the return to be filed in Form GSTR-3 is the final return for taking additional input tax credit as well as discharging of additional tax liabilities after filing of return in Form GSTR-3B. Therefore, last date for availing the input tax credit relating to the invoices issued during the period from July 2017 to March 2018 is the last date for filing of the return in Form GSTR-3 and not GSTR-3B.

Discussions and observations of High Court

Writ-application seeks to quash and set aside the press release dated 18th October 2018 to the extent that the last date for availing input tax credit relating to the invoices issued during the period from July 2017 to March 2018 is the last date for the filing of the return in Form GSTR-3B for the month of September 2018.

Section 16(4) of the CGST Act provides that last date for taking the input tax credit in respect of any invoice or debit note pertaining to a financial year, is **earlier** of due date of furnishing of the return under Section 39 for the month of September following the end of the financial year **or** furnishing of the relevant annual return.

The moot question is, whether the return in Form GSTR-3B is a return required to be filed under Section 39 of the CGST Act. The aforesaid press release is valid and in consonance with Section 16(4) of the CGST Act only if Form GSTR-3B is a return required to be filed under Section 39 of the CGST Act.

Section 39(1) of the CGST/GGST Act provides that every taxpayer, except a few special categories of persons, shall furnish a monthly return in such form and manner as may be prescribed. Rule 61 of the CGST Rules/GGST Rules prescribes the form and manner of submission of monthly return. Sub-rule (1) of Rule 61 of the CGST Rules/GGST Rules provides that the return required to be filed in terms of Section 39(1) of the CGST/GGST Act is to be furnished in Form GSTR-3.

It would be appropriate to state that initially it was decided to have three returns in a month, i.e., return for outward supplies (GSTR-1) in terms of Section 37, return for inward supplies in terms of Section 38 (GSTR-2) and a combined return in Form GSTR-3. However, considering technical glitches in the GSTN portal as well as difficulty faced by the taxpayers it was decided to keep filing of GSTR-2 and GSTR-3 in abeyance. Therefore, in order to ease the burden of the taxpayer for some time, it was decided in the 18th GST Council meeting to allow filing of a shorter return in Form GSTR-3B for initial period. **It was not introduced as a return in lieu of return required to be filed in Form GSTR-3.** The return in Form GSTR-3B is only a temporary stopgap arrangement until due date of filing the return in Form GSTR-3 is notified. Notifications are being issued from time-to-time extending the due date of filing of the return in Form GST- 3, i.e., return required to be filed under Section 39 of the CGST Act/GGST Act. It was notified *vide* Notification No. 44/2018 Central Tax dated 10th September 2018 that the due date of filing the return under Section 39 of the Act, for the months of July 2017 to March 2019 shall be subsequently notified in the *Official Gazette*.

It would also be appropriate to point out that the Notification No. 10/2017-Central Tax dated 28th June, 2017, which introduced mandatory filing of the return in Form GSTR-3B stated that it is a return in lieu of Form GSTR-3.

However, the Government, on realizing its mistake that the return in Form GSTR-3B is not intended to be in lieu of Form GSTR-3, rectified its mistake retrospectively *vide* Notification No. 17/2017-Central Tax dated 27th July, 2017 and omitted the reference to return in Form GSTR-3B being return in lieu of Form GSTR-3.

Order of High Court

The impugned press release dated 18th October 2018 could be said to be illegal to the extent its para 3 purports to clarify that the last date for availing input tax credit relating to the invoices issued during the period from July 2017 to March 2018 is the last date for the filing of return in Form GSTR-3B (for the month of September 2018).

The said clarification could be said to be contrary to Section 16(4) of the CGST Act/GGST Act read with Section 39(1) of the CGST Act/GGST Act read with Rule 61 of the CGST Rules/GGST Rules.

B. Rulings by Authority for Advance Rulings

1. ALCON RESORT HOLDINGS PRIVATE LTD – AAR GOA (2019-TIOL-209-AAR-GST)

Facts, Issue involved and Query of the Applicant

Applicant is having an established centre under the name and style "Devaaya Ayurveda & Nature Cure Centre" for providing health care treatment services to the patients through Ayurveda, Naturopathy and Yoga. It provides health services to both international as well as Indian patients for Neuro muscular problems, post chemotherapy, post radiotherapy treatment, skin problem like psoriasis and chronic allergies, metabolic issues like obesity and other life style problems and orthopaedic problems like rheumatoid arthritis, osteoarthritis etc.

Applicant has sought advance ruling for the following:

1. *Whether the applicant qualifies as clinical establishment?*
2. *Whether the services provided by the applicant qualify to be health care services which are exempted under Entry No.74 of the Notification No. 12/2017-Central Tax?*

Discussions by and observations of AAR

Notification No. 12/2017-Central Tax defines clinical establishment to mean a hospital, nursing home or any other institution by whatever name called, that offers services or facilities requiring diagnosis or treatment in any recognised system of medicines in India, or a place established as an independent entity.

The said notification further defines health care services to mean any service by way of diagnosis or treatment in any recognised system of medicines in India and includes services by way of transportation of the patient to and from a clinical establishment, but does not include hair transplant or cosmetic surgery except, when undertaken to restore or to reconstruct anatomy or functions of body affected due to congenital defects, development or trauma.

In the instant case, the applicant provides health care services by way of appropriate diagnosis, appropriate medicines as well as relevant consumables or implants as part of treatment under supervision of qualified doctors till discharge.

Therefore, stay for treatment, supply of medicines, consumables and implants used in the course of providing health care services to in-patients is undoubtedly naturally bundled in the ordinary course of business. It would be considered as composite supply and eligible for exemption under the category of 'health care services'.

Ruling of AAR

The applicant qualifies to be a clinical establishment and the services offered/provided by the applicant qualify to be the health care services. The intra-State supplies of the said services attract NIL rate of tax as per Sl. No. 74 of the Notification No. 12/2017-Central Tax dated 28th June, 2017.

2. DAIMLER FINANCIAL SERVICES INDIA PRIVATE LIMITED - AAR TAMIL NADU (2019-TIOL-212-AAR-GST)

Facts, Issue involved and Query of the Applicant

Applicant (hereinafter referred to as 'DFSI'), registered as a Non-banking Financial Institution, is engaged in the activities of 'leasing and finance' of commercial and passenger vehicles to end-customers. Customers who purchase Mercedes Benz India (MB India) cars from the authorized dealers may require financing. DFSI acts as a financer and provides loan to customers of MB India at **lower rates** as decided between DFSI and MB India. The differential interest [market rate (-) rate offered to customers] is paid by MB India to DFSI. This amount paid is termed as **interest subvention or alternatively interest subsidy**. The subvention amount is identified and paid upfront by MB India to DFSI. Recognition of proportionate interest subsidy as income of DFSI is done over the tenure of the loan provided to the customer.

DFSI has sought Advance ruling on the question as to *whether the interest subvention income received by DFSI from Mercedes Benz India Private Limited (MB India) to reduce the effective interest rate to the final customer is chargeable to GST.*

Applicant's submissions

Applicant submitted that interest income is exempt *vide* entry No. 28 of Notification No. 9/2017-Integrated Tax (Rate) dated 28th June 2017. As per definition of "interest" in para 2 of this notification, it is not necessary that only the borrower pay interest.

As per definition of "consideration" under CGST Act read with Indian Contract Act, 1872, any person may pay consideration. Subvention payment or discount is consideration in the form of interest paid by MB India on behalf of its customer.

Interest subvention income is interest income received from a person other than the borrower. Both the GST law and the Indian Contract Act, 1872 recognize that consideration for a transaction can flow from anybody. Subvention income earned from a party other than the borrower represents consideration for the borrowing - that is interest.

Discussions and observations of Authority

AAR observed the MOU dated 25-5-2016 between DFSI and MB India which was renewed till 31-12-2018. As per this MOU, they shall work together to promote and facilitate sales of Mercedes-Benz vehicles in India. DFSI has agreed to extend loans to those customers referred by MB India/its dealers. DFSI shall be the first choice financier for financing customers referred by MB India for purchasing Mercedes-Benz Vehicle on a non-exclusive basis. There will be a separate invoice for this additional subvention.

As per Section 2(31) of CGST Act, consideration for any supply includes payment made or to be made. In this case, for the supply of credit granting services by DFSI to the buyer, the buyer has to pay interest only at the rate agreed to in the agreement under "Rate of Interest per Annum" which does not include the interest subsidy from MB India.

As per Section 15 of CGST Act, the value of this supply is the transaction value, which is the price actually paid or payable for the said supply, which is again only the amount as per the interest rate specified equal to 'Net Applicable Fixed Interest Rate'. There is no other amounts payable by the buyer as per the agreement terms.

Hence, the stand of the applicant that the interest subvention amount given by MB India to DFSI is a part of the consideration for the transaction between DFSI and buyer is not correct as the buyer is under no obligation to pay this amount equivalent to the interest subvention to DFSI.

In order to enable DFSI to provide the competitive rates, MB India will subvent the interest to be charged to the final customer. DFSI is showing this amount received from MB India as "Revenue from Operations" in the audited financials.

Section 7 of CGST Act defines scope of supply to include–

(a) *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;*

The agreement between DFSI and MB India is for the furtherance of the business of lending of DFSI as they are the preferred financiers of MB India's vehicles. Customers buying MB India's vehicles would prefer to take out a loan from DFSI because of their lower interest rates offered. Therefore, this transaction between DFSI and MB India is a 'Supply' under Section 7 of CGST Act.

In the instant case, DFSI is agreeing to provide vehicle loan to buyers of MB India's vehicles at a lower interest rate as decided between DFSI and MB India. It also agrees to provide better customer luxury experience, structured insurance product offerings with claims processing within minimum turnaround time, tailor made products, quick loan approvals, maintain customer relation etc. as per the MOU between FSI and MB India. Hence, the supply of service by DFSI to MB India is covered under SAC 999792 as 'Other miscellaneous Services, agreeing to do an act', etc. chargeable to GST at rate of 18%.

Ruling of AAR

Interest subvention income received by applicant from MB India to reduce the effective interest rate to the final customer is chargeable to GST. It is a supply under SAC 999792 as 'Other Miscellaneous Services' chargeable to GST at rate of 18%.

3. KONKAN LNG PRIVATE LIMITED – AAR MAHARASHTRA (2019-TIOL-201-AAR-GST)

Facts, Issue involved and Query of the Applicant

Applicant is in business of Liquefied Natural Gas (LNG) **regasification** on which it duly discharges GST liability. Regasification of LNG is being carried in applicant's Liquefied Natural Gas regasification plant. The said plant is strategically located near wet-land wherein LNG (raw material) stored in modified cargos reaches plant through captive jetty/ship for regasification.

Usually, area where LNG cargoes are unloaded from captive jetty/ship, **"breakwater wall"** is constructed for safe unloading of LNG cargoes and protecting jetty/ships from getting damaged by high waves and tides.

In present case, there was incomplete breakwater wall due to which clearing authority was not granting clearances for berthing of ship and unloading of cargoes unless height of the waves were less than 0.5 meter. This caused restriction in smooth working of business and therefore, out of business expediency, applicant floated international tender for detail engineering and construction of breakwater wall including dredging work, placing core as well as secondary material and installing acropods.

The said breakwater wall work is "works contract" on which contractor will charge GST.

Applicant has sought an advance ruling on following questions:

1. *Whether it can avail ITC of GST charged by supplier on construction of Breakwater wall (immovable property), which is an integral part of existing jetty and very much required for the purpose of safety and making existing jetty fully workable as an all-weather jetty and hence improves the operation efficiency of the applicant;*

2. *Whether said works contract service, to be procured by applicant, is predominantly earthwork (constituting more than 75%, of the value of works contract) and gets covered under serial No. 3(vii) of N/No. 11/2017-CT (R) dated 28-6-2017 as amended by N/No. 31/2017–CT (R) dated 13-10-2017?*

Applicant's submissions

Section 17(5)(c)/(d) of the CGST Act, 2017 blocks availment of ITC on any goods/services used for purpose of construction of immovable property **excludes** goods/services used for construction of Plant & Machinery ('P&M').

"Breakwater wall" even though immovable property is a P&M which allows uninterrupted receipt of LNG (raw material) in course and furtherance of business. P&M is not defined u/s. 17 of CGST Act. Hence, it relied on various judicial judgments which states:

i. *Dry dock and wet dock created for ship is P&M and not building [Mazagoan Dock Limited - reported in 191 ITR 460-HC];*

ii. *Building can be treated as plant if it is well planned and constructed to serve special technical requirement [Karnataka Power corporation as reported in (2001) 247 ITR 268 (SC) = 2002-TIOL-950-SC-IT-LB];*

iii. *Operation theatre in a hospital building is not a civil structure simplicitor but necessarily a part of running a hospital [Dr. B. Venkata Rao Hospital 243 ITR 81 (SC) - 2002-TIOL-522-SC-IT]*

In view of the above submissions and the definition of the terms apparatus and equipment, the applicants submitted that the acropads (an interlocking device) to be placed are apparatus which are used for a specific purpose of effective working of breakwater wall. Hence, Applicant should be allowed to take ITC on works contract to be availed for construction of breakwater wall.

Department's submissions

Explanation to section 17(6) of the CGST Act defines "Plant and Machinery" in which it specifically excludes "civil structure". The Breakwater wall is a "civil structure" which gets excluded from definition of plant and machinery.

Further, even in judicial judgment on which applicant is relying states:

*"In order for a building or concrete structure to qualify for inclusion in the term plant, it must be established that it is **impossible for the equipment to function without the particular type of structure."***

In present case, even though applicant had incomplete breakwater wall it was having fully functional LNG regasification plant so it cannot be proved that it is impossible to function without complete breakwater wall. Hence, breakwater wall being "civil structure" on construction of which ITC of inputs/input service is blocked by section 17(5) of CGST Act.

Observations of AAR

The applicant has agreed that breakwater wall is "immovable property". Now the question arise whether breakwater wall can be considered as "P&M".

The explanation of section 17(6) of the CGST Act defines as:

"Plant and Machinery means apparatus, equipments and machinery fixed to earth by foundation or structural

support that ***are used for making outward supply of goods or services or both*** *and includes such foundation and structural support but excludes:*

i) Land, Building or any other civil structure

ii) …

iii) …….”

The breakwater wall can be considered as a civil structure. As per definition, the apparatus, equipment and machinery should be used for making outward supply of goods and service or both. In present case, the breakwater wall will be facilitating the safe receipt of raw material and not rendering outward supply.

Further, even without breakwater wall it is possible to operate LNG regasification plan hence it cannot be said breakwater well is integral part of plant. Hence, applicant is not eligible to take ITC of construction of breakwater wall.

In respect of question 2, authority did not answer based on following ground:

As per section 95 of the CGST Act, the term 'advance ruling' means a decision provided by this authority to the applicant on matters or question specified u/s. 97 in relation to the supply of goods or services or both being proposed to be undertaken by applicant.

Since in this case applicant is receiver and not a provider of works contract service, the issue is not within purview of this authority, therefore, this question is not answered.

Ruling of AAR

In respect of question 1, applicant is not entitled to ITC as same is block u/s. 17(5)(d) of the CGST Act.

In respect of question 2, since applicant is a recipient of service and not a service provider, the authority restrain to answer the same.

4. MAYANK JAIN – AAR MAHARASHTRA (2019-TIOL-229-AAR-GST)

Facts, Issue involved and Contention of Applicant

Applicant is an individual exploring business opportunity in providing marketing and advisory services in relation to the Employee Based Immigration. EB-5 programme envisages that an investor is eligible to permanent residence in USA subject to an investment of USD 5,00,000. Applicant wants to provide certain services in the nature of marketing and intelligence to the 'Consultant Manager' acting for the Regional Centre or Company enabling them to receive investments from prospective investors.

The scope of work under this Agreement titled as "Foreign Immigration Advisor Agreement" is as below:

iv. Market analysis;

v. Market EB-5 programme in India;

vi. Address queries of consultant manager;

vii. Handholding services; etc.

Consideration for such services will be provided upon successful investment/repatriation by the investor.

Applicant has sought advance ruling on the following:

i. Whether Marketing services and Handholding services provided to the consultant manager constitutes a supply of 'Support Services' classified under SAC 9985 or 'Intermediary service' classified under SAC 9961/9962 or any other heading?

ii. Whether the Marketing services and Handholding services provided by the Applicant will be Export of services as defined under section 2(6) of the IGST Act, 2017?

Applicant's submissions

Intermediary is a person who is a broker, agent or any other person by whatsoever name called. 'Any other name called' takes the colour from preceding term i.e. doctrine of *ejusdem generis.* Applicant is not acting in representational capacity on behalf of either consultant manager or the individual. He provides services on a principal-to-principal basis to the consultant manager.

Applicant is nowhere providing services between two or more persons. He is providing services to consultants who are paying fees. The job of applicant is only to conduct marketing services. It cannot be termed as intermediary. His services are in nature of business support services.

Supplier is located in India and service recipient is outside India. Place of supply u/s. 13(2) for business support services falls outside India. Applicant will be paid in foreign exchange for the services rendered by him. All requirements for export of services under GST are satisfied. Therefore, marketing and hand-holding services are export of services under GST legislation.

Discussions by and observations of AAR

AAR observed that the applicant's scope of business included planning and conducting marketing activities for the Consultant Manager. It includes preparing report, making plans, market intelligence, compiling list of prospective investors for the consultant manager. Once an Indian investor is interested in making investment under the EB-5 Scheme he contacts the applicant who provides services to the Indian Investor and facilitates meeting/contact between the Consultant manager and the Investor. For that purpose, the consultant appoints an agent or an intermediary. The agreement however may not call the applicant as an agent or middleman but his services are in the nature of a middleman who facilitates meeting between the Indian investor and the Consultant manager. Applicant has contended that he is providing only marketing services to the Consultant. However, the applicant acts as a facilitator between the Consultant manager and the investor. Applicant is squarely providing intermediary services in the name of marketing service.

The next service provided by the applicant is handholding i.e., to help the investor fill up forms, helps in preparation of various documents on behalf of the consultant manager who ultimately identifies the appropriate and profitable projects for investment. This is in fact intermediary services in name of handholding services.

Section 2(13) of the IGST Act defines 'intermediary' to means a broker, an agent or any other person, by whatever name called, who arranges or facilitates the supply of goods or services or both between two or more persons but does not include a person who supplies such goods or services or both on his own account. Applicant facilitates investment/permanent residence advisory service provided by consultant manager to investor. It arranges/facilitates meetings between investors and consultant managers. Applicant does not provide services on his own account. He squarely falls under the definition of Intermediary for both – marketing and handholding services.

Services provided by applicant to consultant manager falls under section 13(8) of IGST Act. Hence place of supply of such services is within India. Therefore the services rendered by the applicant is not 'export of service' as condition of section 2(6) of the IGST Act, 2017 for export of services is not fulfilled.

Ruling of AAR

In respect of question raised by the applicant, 'Marketing services' and 'Handholding services' provided by the applicant to the consultant manager constitutes a supply of "Intermediary Services" classified under SAC 9985.

Also, the 'Marketing and Handholding services' provided by the applicant to the management consultant is not export of services.

5. ROTARY CLUB OF MUMBAI QUEENS NECKLACE – AAR MAHARASHTRA (2019-TIOL-203-AAR-GST)

Facts, Issue involved and Contention of Applicant

Applicant/Club is an unincorporated association of individuals. The club is affiliated to Rotary International, a worldwide organisation. Club brings together dedicated individuals to exchange ideas, build relationships and take action. The Club uses generous donations to fund projects by Rotarians and other partners in communities around the world. The main purpose of the Club is to promote integrity and advance world understanding, goodwill and peace. In addition, they work to fight diseases, provide clean water, sanitation, hygiene, support education, etc.

The members come together to form a Rotary Club and the same is not a service club. The Club has an annual budget of expenses. Money is pooled by the members in equal share. It is not for profit institution. It does not render commercial service to its members nor does it render services to outsiders for a fee. The amounts collected by way of fees are pooled together and are not expected to generate any surplus. Club has not been formed to give any facilities or services to its members.

Applicant seeks advance ruling on following questions:

i. *Whether subscription fees and admission fees collected from members is liable to GST?*

ii. *If answer to above is yes, whether Input Tax Credit (ITC) on banquet and catering services be availed?*

Applicant's submissions

Harmonious reading of provisions of supply, leviability and consideration under GST provides that where a consideration is involved in a transaction, recipient is the person who pays consideration to supplier. Hence, two different persons have been envisaged in law to tax a transaction as a supply.

Term 'person' as defined under GST does not contain deeming fiction to treat club and its members as different persons. Merely because association of person is included in definition of person it does not imply that members of such association are different persons. Article 366(29A) enables to tax deemed sales. It does not enable to tax service as deemed service.

Members come together to form a Rotary Club, It is not an entertainment club or recreational service Club. The events are held by Club for holding lectures and fund raising. The Club is not formed to provide services to members. Holding a meeting at good venue does not make it taxable.

Applicant further relied on decision of Maharashtra AAR in case of Lions Club of Kothrud, Pune wherein AAR has held that there is no supply *qua* the fees received. There is no occasion to visit the definition of supply under GST. Club is not liable does not render any supply for the purpose of GST.

Discussions by and observations of AAR

Applicant has relied on case of 'Lions Club of Poona Kothrud' wherein Maharashtra AAR has ruled "Club is not formed to provide any supply of goods or services to its members *qua* the fees received from them. Since there being no supply *qua* the fees received, there arises no occasion to visit the definition of 'Supply' under the GST Act."

AAR observed that the Appellate Advance Ruling Authority overruled the Advance Ruling in the case of 'Lions Club of Poona Kothrud'.

Observations of AAAR are as under:

- As per the definition of person under the CGST Act, 2017, the club and its members are two different person.
- GST Law has a very wide scope for services, which will cover all activities other than goods, money or securities. Therefore, the activities of the respondent (Lions Club) like the leadership programme, meeting sessions conducted for the members are considered as services.
- Also, the membership fees collected from the members satisfy the definition of consideration as defined under section 2(31) of the CGST Act, 2017.
- The Lions club has therefore fulfilled both the conditions of Section 7 (Supply) of the CGST Act, 2017. First condition being supply made in lieu of consideration and second condition of such supply being in the course or furtherance of business.

  [As business includes provision by club, association, society, or any such body (for a subscription or any other consideration) of the facilities or benefits to its members.]
- Therefore, GST is payable on the membership fees received by the Lions Club on the services provided by them to their members.

AAR concluded stating that since the applicant has heavily relied on the AAR of Lions Club of Poona, Kothrud and have submitted that the applicant's facts are similar to the case of Lions Club of Poona, the amount collected as membership subscription and admission fees from members is liable to GST as supply of services.

As per section 17(5) of CGST Act, ITC shall not be available in respect of the following:

i. ***Food & beverages,*** *outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, leasing renting or hiring of motor vehicles, vessels or aircrafts referred to in clause (a) of clause (aa) except when used for the purpose specified there in, life insurance and health insurance.*

Provided that the ITC in respect of such goods or services or both shall be available where an inward supply of such goods or services or both is used by a registered person for making as outward taxable supply of the same category of goods or services or both or as element of taxable composite or mixed supply.

ii. ……………………………………..

iii. ………………………………………..

ITC of food and beverages is specifically disallowed u/s. 17(5) except where it is used for making an outward taxable supply of same category of goods or services. Provisions of section 17(5)(b) are crystal clear. Unless it is satisfied the applicant is not entitled to ITC of food and beverages and outdoor catering.

Ruling of AAR

In respect of question raised by applicant, the amount collected as membership subscription and admission fees from members is liable to GST as supply of services.

Further, applicant is not eligible to claim ITC of tax paid on banquet and catering services for holding meetings or events.

6. TVH LUMBINI SQUARE OWNERS ASSOCIATION - AAR CHENNAI (2019-TIOL-226-AAR)

Facts, Issue involved and Contention of Applicant

Applicant is a residential welfare association registered under GST legislation. The society consists of 9 residential blocks. There are 448 flats in total and each block contains an approximate of 50 flats. Applicant collects maintenance charges on a quarterly basis at ₹ 3.50 per sq. ft. per month. They are further claiming exemption of ₹ 7,500/- as per S. No. 77 of Notification 12/2017-Central Tax (RATE) dated 28-6-2017 in respect of those members whose contribution toward maintenance charges does not exceed 7,500/-per month.

Applicant has sought a ruling on the question as to whether applicant is liable to pay GST on amount in excess of ₹ 7,500/- or on entire amount if the monthly charges payable by a Member of the Association exceeds ₹ 7500/- per month?

Applicant's submissions

Exemption under Sr. No. 77 of the cited notification is to the extent of ₹ 7,500/- per month, collected from the members for sourcing of goods or services from a third person for the common use of the members in a housing society of a residential complex. In view of above, if the monthly maintenance charges are ₹ 8,000/- per month, the liability of GST will only be on difference of ₹ 500/-and not on the entire amount of ₹ 8,000/-. This can be inferred from the language of exemption Notification No. 12/2017-CT (Rate) wherein the words "**Up to an amount of five thousand rupees per month per member**" which was later substituted to "Seven thousand and five hundred" [as per Notification No. 2/2018-Central Tax (Rate)]. Hence, the applicant is of the view that, the exemption is up to ₹ 7,500 per month and it does not lay down that this exemption would be lost, if the amount exceeds ₹ 7,500 per month.

Discussions by and observations of AAR

Applicant procures various services such as Facility Management Services, De-Mosquitoes Solutions, Maintenance of Swimming Pool, Servicing and Maintenance of lifts. Applicant collects maintenance charges from the members towards maintenance.

AAR by referring to the relevant entry of the notification noted that only services, which exactly match the description of exemption notification, are covered under the Sr. No. 77(c) of said Notification.

In the instant case, this exemption is applicable only if the service provided by applicant to its members by way of reimbursement of charges or share of contribution, for sourcing of goods or services from a third person for the common use of its members is up to an amount of ₹ 7,500 per month per member.

In the event the charges or share of contribution goes above ₹ 7,500 per month per member, such service will not fit the above description and hence, exemption shall not be available. It will be fully chargeable to GST at the applicable tax rate.

There is no option to the taxpayer to pick and choose from the description of the services mentioned in column (3) to make any service partly applicable to the notification and partly chargeable.

Ruling of AAR

Services provided by applicant to its member by way of reimbursement or charges for sourcing of goods or services from a third person exceeding ₹ 7,500/- will not be entitled to exemption. GST at appropriate tax rate shall be levied on full amount of reimbursement.

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INDIRECT TAXES

CA Rajiv Luthia & CA Keval Shah

Service Tax – Case Law Update

1 *Airvent Systems Private Limited vs. Commissioner of GST & CE, Chennai*

2019-VIL-409-CESTAT-CHE-ST

Background Facts of the case

The appellants are registered with the Service Tax Department under the categories of Maintenance or Repair Service, Erection Commissioning and Installation Service, Consulting Engineering Service and Works Contract Service. On verification of records, it was seen that they had not paid Service Tax on Co-consultancy Services rendered by them and had also short paid Service Tax on the services provided towards Erection, Commissioning and Installation Services.

Accordingly, a Show Cause Notice was issued for such short payment for Erection Commissioning and Installation service and Co-Consultancy Services, which was adjudicated by the Commissioner (Appeals) after directing to re-quantify the demand under Works Contract Service.

Arguments put forth

The Appellants submitted as under:

a) The Ld. CCE (Appeals) has travelled beyond the SCN as well as the order passed by the Original Authority to confirm the demand under Works Contract Service, whereas the SCN was issued under Erection Commissioning and Installation Services.

b) The period of dispute is from 2005-06 to 2007-08. The CCE (Appeals) has erroneously concluded that for the period up to 1-6-2007, the appellant is required to pay Service Tax on the entire value with permissible abatement and for the period after 1-6-2007, the appellant would be liable for payment of Service Tax under Works Contract Service as per Composition Scheme. He ordered for re-quantification of the demand in such manner.

c) They relied upon the decision in the case of Commissioner of *C.Ex. & Cus., Kerala vs. M/s. Larsen & Toubro* reported in 2015 (39) S.T.R. 913(S.C.) - 2015-VIL-88-SC-ST to submit that prior to 1-6-2007, the levy of Service Tax on such composite contracts cannot sustain. Even thereafter, the Service Tax demand cannot sustain under the category of 'Erection, Commissioning and Installation Services', as held by the Tribunal in the case of *M/s. Real Value Promoters Pvt. Ltd. & Ors. vs. Commissioner* *of G.S.T. & Central Excise, Chennai* reported in 2018-TIOL-2867- CESTAT-MAD - 2018-VIL-648-CESTAT-CHE-ST.

d) As far as Co-Consultancy Services are concerned, there were several decisions passed by the Tribunal holding that when the main contractor has discharged Service Tax, there is no liability on the sub-contractor to pay the Service Tax. Later, the Board *vide* Circular dated 23-8-2007 clarified that the subcontractor has also to pay Service Tax. The appellant had not discharged Service Tax during the relevant period only because of the *bona fide* belief that the main service provider was discharging the Service Tax and that therefore, the appellant had no liability to pay the Service Tax. It was also stated that the SCN issued invoking the extended period of limitation cannot sustain in case of Co-consultancy services.

The Respondents submitted as under:

a) The appellant was bifurcating the value of services rendered and supply of materials and discharging Service Tax only on the service portion. That for discharging Service Tax, the appellant has to take the entire value of the contract into account and thereafter deduct the eligible abatement.

b) With regard to the issue on Co-consultancy Services, the appellant had not discharged Service Tax for the disputed period, which is from 2005-06 to 2007-08. Even though the appellant has rendered services only as a Co-consultant, is liable to discharge Service Tax on the amount received by them for rendering such services. The Department has clarified the said issue as to the liability of the Sub-contractor to pay Service Tax *vide* Master Circular No. 96/7/2007-ST dated 23-8-2007.

Decision

a) For the period prior to 1-6-2007, the demand of Service Tax for such composite contracts cannot sustain as per the decision of the Hon'ble Supreme Court in the case of *M/s. Larsen & Toubro Ltd. (supra)*. For the period post 1-6-2007.

b) When the demand in the SCN is under Erection, Commissioning and Installation Service, the confirmation of demand under Works Contract Service is highly erroneous and unsustainable

c) The Tribunal in case of *M/s. Real Value Promoters Ltd. (supra)*, has held that the demand of Service Tax under Erection, Commissioning and Installation Services cannot sustain for composite contracts for the period post 1-6-2007.

d) The appellant has submitted that they were under the *bona fide* belief that as a Co-consultant, they are not liable to pay Service Tax since the main service provider was discharging Service Tax. Indeed, there were decisions in favour of the assessee during the disputed period wherein it was held that when the main contractor has discharged Service Tax, the sub-contractor has no liability to pay Service Tax. The Board in its Circular dated 23-8-2007 had occasion to clarify the issue that Service Tax has to be discharged by the Sub-contractor also. Since this issue involves interpretational issues, the extended period of limitation cannot be invoked in present case.

e) Accordingly, the appeal was allowed.

2 ***UP Gujarat Freight Carrier vs. Commissioner of CGST & CE***

2019-VIL-408-CESTAT-DEL- ST

Background Facts of the case

The appellant was served with a SCN dated 13-9-2017 proposing the recovery of service tax amounting to ₹ 1,52,430/- along with the interest and the penalty for allegedly not discharging the liability for rendering the services as that of transport of goods by road and renting of immovable property during the period 2012-13 to 2015-16.

The said proposal was confirmed *vide* the Order in Original and aggrieved by the same, the assessee preferred an appeal before Commissioner (Appeals). The appeal was dismissed by the Commissioner (Appeal) for non-payment of mandatory pre-deposit of 7.5% of the service tax involved in this case

Arguments put forth

The Assessee as Appellants submitted as under:

a) The appellant had deposited part of the amount during the course of investigation and balance part after the Order under challenge *vide* Challan dated 28-8-2018. The total amount deposited is equal to 7.5% of the demand confirmed by the Order-in-Original.

b) The Appellants has also relied upon the Circular of Ministry of Finance bearing No. 984/08/2014–CX dated 16-9-2014 about the payment made during the course of investigation or audit, prior to the date on which Appeal is filed can be considered to be the deposit made towards fulfilment of pre-deposit.

The Respondent submitted as under:

a) It is submission of the Department that amount deposited after the Order-in-Original has duly been considered by Commissioner (Appeals) however, the said amount was short of 7.5% of the demand confirmed that the Appeal has rightly been dismissed.

Decision

a) Two payments have been made by the appellant with respect to the impugned demand as is apparent from the copies of Challans annexed on record. There is no denial to these nor even to the fact that both these payments are in lieu of the demand in question.

b) The perusal makes it abundantly clear that the 10% of the amount of demand confirmed as is mandatorily to be deposited by the appellant at the time of filing the Appeal before this Tribunal is a mandatory deposit in terms of Section 35F of the Central Excise Act. However, any payment made by the appellant during the course of the investigation has to be adjusted against the said percentage of mandatory deposit. In view of the above admissions, the amount which stands deposited.

c) The amount admittedly already stands deposited. Hence, we are of the opinion that the Commissioner (Appeals) has committed an error while dismissing the Appeal to be barred by Section 35.

d) Accordingly, the appeal filed by the Appellants was allowed by way of remand back to Commissioner (Appeals) to decide the matter on merits.

3 ***Ess Infraproject Private Limited vs. Union of India & Others***

2019-VIL-313-BOM-ST

Background Facts of the case

This petition seeks a declaration that Respondents do not have power under Rule 5A of the Service Tax Rules, 1994 read with Section 174(2)(e) of the Central Goods and Services Tax Act, 2017 (CGST Act) to conduct audit for the period October 2013 to June 2017 i.e. prior to the introduction of CGST Act on 1st July, 2017.

Arguments put forth

The Petitioners submitted as under:

a) It is submitted that for interim relief is that various courts i.e. Gujarat High Court in the case of *OWS Warehouse Services LLP vs. Union of India,* 2018 (19) G.S.T. 27 (Guj.) - 2018-VIL-463-GUJ, the Delhi High Court in the case of *M/s. T. R. Sawhney Motors Pvt. Ltd. vs. Union of India* in Writ Petition(C) No.2138 of 2019 and Jharkhand High Court in the case of *M/s. Sulabh International Social Service Organization, (Jharkhand State Branch) vs. Union of India* in Writ Petition (T) No. 1599 of 2019 - 2019-VIL-134-JHR-ST have in respect of identical challenge granted interim relief to the petitioner.

b) It is also submitted that in any event, the Delhi High Court in *Mega Cabs Pvt. Ltd. vs. Union of India* 2016 (43) S.T.R. 67 (Del.) - 2016-VIL-282- DEL-ST has held that Rule 5A of Service Tax Rules, 1994 is ultra virus to parent Act i.e. Finance Act, 1994. Therefore, bad. Thus, Rule 5A of the Service Tax Rules, 1994, it is submitted, cannot be enforced.

Decision

a) The issue of the saving of Rule 5A(2) of Service Tax Rules, 1992 on introduction of CGST Act, 2017 is an issue that requires detailed consideration. This would be appropriately done at the final hearing.

b) Thus, granting of interim relief at this stage would tantamount to granting final relief at the stage of admission. The Respondents seeks to carry out audit in terms of Rule 5A of Service Tax Rules, 1994 and Section 174 of the CGST Act for the period prior to the introduction of CGST Act. Grant of interim relief at this stage would prevent the respondents from carrying out audit as permitted under Rule 5A of Service Tax Rules, 1994 and Section 174(2)(e) of the CGST Act.

c) At the final hearing, if the challenge is negative, there would be a delay in conducting the audit which would then result in difficulty as papers and persons who are in a position to be respond to audit queries may not be available and/or their memories may fail. Besides any action to be taken pursuant to the audit may become time barred, if not already so. No prejudice will be caused to the petitioners if it subjects itself to audit at this stage. If any further proceedings are taken on the basis of audit report against the petitioners, they are at liberty to move the Court for interim relief. Such an application, if made which would be considered at that point of time by the court to which served an application is made

d) Accordingly the petition was admitted, however without any interim relief to the Petitioners.

4 ***M/s. Wartsila India Ltd. vs. Commissioner of Service Tax***

2019-TIOL-2006-CESTAT-MUMBAI

Background Facts of the case

The appellants are engaged in the operation of power plants and generation of electricity and have entered into operation and maintenance agreements with various customers at different locations. The customers have captive power plants for generation of power which is used to manufacture dutiable products, majority of the customers belonging to the steel and automobile industry. The appellants are required to operate and run the plant to generate power within the norms set in the agreement, the agreement also imposes penalty in case where the consumption of the fuel, lube oil, spare parts etc. exceeds the standard norms set. The appellants charge "operation fee" and "Maintenance fee" from their customers & pay service tax on the maintenance fees collected, even though they are of the opinion that it was not liable to service tax. The revenue contented that power plant is an immovable property & operation thereof would amount to "management" which is taxable under the category of "maintenance & repair service"; the appellants started paying service tax on the same as the customers were entitled to credit of the same and the appellants didn't wanted to litigate as it was revenue neutral situation. The revenue issued SCN to the appellants for recovering the service tax under the head "Management, maintenance or repair services" along with penalties u/s. 76, 77 & 78 of the FA, 1994. Hence, the impugned appeal.

Arguments put forth

The Appellants submitted as under:

a) The word "management" takes its colour from "maintenance" and "repair", hence it would not include operation within its scope. By applying the principle of Noscitur A Sociis , the term "management" would take the colour from the words "maintenance & repair" and therefore "management" would not cover within its scope the activity of generation of electricity, by running the power plant. The impugned order is liable to be set aside.

b) The most common concept of management involves getting things done through and with people. Hence, the term "management of any organisation" appearing in section 65 of the FA, 1994 would not mean the entire range of activities in the organisation. They generally regulate, supervise, direct and control the activities of the other functionaries in the organisation. The appellants run the entire plant themselves, hence by no stretch of imagination it can be construed management of immovable property.

c) The appellants themselves operate the plant to generate power. The other activities such as maintenance, repair etc. are incidental to the main activity. The said activities are in the nature of self-service. In view of the same, no service tax must be demanded from the appellants & the impugned order is liable to be set aside.

d) The dispute is no longer *res integra* and is settled in favour of the appellants in the case of *CLP Power India vs. CST* wherein the Hon'ble Mumbai Tribunal has decided in the favour of the assessee.

e) The decision of Hon'ble Madras Tribunal in the case of *CMS Operations & Maintenance Co. Pvt. Ltd.,* held that the argument of the appellants that they maintained only the plant and the taxable service of maintenance or repair of goods/ equipment covered by the Act were done by the suppliers of the equipment under warranty or Annual Maintenance Contract (AMC) is reasonable and merits acceptance. If the appellants undertook these activities they had rendered the service to themselves and not to another person. Therefore, no liability is incurred by the appellants on this account." The dispute in the present case is squarely covered by aforementioned decisions and thus, the impugned order is liable to be set aside.

Decision

a) Analysing the activity undertaken by the appellants *vis-à-vis* the definition of "Management, Maintenance or Repair Service" u/s. 2(64) of the Act, it is clear the appellants are basically operating the power plants on behalf of their customers. As submitted by the appellants, management would pre-suppose activities like regulating, supervision, direction and control of the activities of the others functionaries in the organization. But in this case, there is no such activity undertaken by the appellants. They are only operating the power plants. It appears that the appellants are not managing the plant for others, in fact, they are themselves operating the plants. Other activities such as maintenance etc., are incidental to the main activity of generation of electricity. The said activities are undertaken for smooth functioning and operation of the plant. In effect, the maintenance part of it, the activities are in the nature of self service to the appellants themselves. However, the appellants are discharging Service Tax on the amounts received as maintenance fee. Therefore, the service rendered by them would not fall under the category of "maintenance or management of immovable property".

b) Further the issue is no longer *res integra.* It has only been decided in the case of *CLP Power India Pvt. Ltd.* vs. *CST,* Mumbai in favour of the assessee. Further, we find that Tribunal in the case of *Operational Energy Group of India Pvt. Ltd.* vs. *CST*, Chennai has held that "the activity would not fall under 'management of immovable property'.

c) The argument of the appellant is not without substance. The major activity in the power plant is production of electricity which is an excisable product. Further, activity of production of electricity cannot be equated with management of immovable property. The management, if any, of the power plant is done by the appellants and is only incidental to the activity of generation of electricity. Thus, it is very much clear that management of immovable property does not include operation activities. In addition, it cannot be said that the appellants are doing management service for the reason that the management service is done by appellants to themselves and not to any other person. The appellants are operating the power plant to generate electricity on behalf of the owner for supplying the same.

d) The appeal was allowed and consequential relief was granted to the assessee.

CORPORATE LAWS

Company Law Update

Janak C. Pandya,
Company Secretary

1 ***Shri Santosh Meenakshi Textiles Pvt. Ltd. vs. Registrar of Companies, Tamil Nadu. Coimbatore***

National Company Law Appellate Tribunal, New Delhi. Company Appeal (AT) No. 335 of 2018. Judgement dated 1st July, 2019.

For the purpose of applicability of CSR provisions, the term "net profit" of INR 5 crore in any of the 3 (Three) preceding year under section 135(1) shall be calculated as per Section 198 of Companies Act, 2013 ("CA13"), which means "Net Profit before tax".

Brief Note

The appeal has been filed by Shri Santosh Meenakshi Textiles Pvt Ltd. ("Appellant") under section 421 of the CA13. The appeal is against the impugned order of National Company Law Tribunal, Chennai. ("NCLT'). The facts are as follows.

1. The Appellant has made net profit above INR 5 crore before tax for the financial year ended March 31, 2014.
2. The appellant has not constituted CSR Committee or approved the CSR Policy. Further, it has not spent 2% of average net profit on CSR.
3. Upon review of Board report, RoC has issued show cause notice to the appellant as to non-compliances of section 135(1), 135(5) and section 134(3) of the CA13.
4. The appellant has replied that section 135 is not applicable and thus no requirement of forming CSR policy or constituting CSR Committee or spending CSR money. Since, section 135 is not applicable, the provisions of section 135(3)(o) as to making disclosure on CSR policy etc. in Board report is also not applicable.
5. The appellant has filed an application u/s. 131 as to revision of the accounts before NCLT.
6. It has submitted before the NCLT, that threshold for CSR is "net profit after tax" as per section 135(1) and hence same is not applicable to it.
7. Further, since the last 3 (three) years' average profit is negative as per section 135(5), no amount could be allocated towards CSR spending and hence provisions of section 135 are not attracted.

8. Being a new Act, appellant did not understand the provisions clearly and hence did not disclose the composition of CSR Committee and CSR Policy.

In reply, RoC has submitted that the ignorance of law is not an excuse. Further, appellant should comply with the CSR provisions for the FY 2014-15. It also stated that it disagrees with the appellant's contention as to non-applicability of section 135(1) since the average net profit for the 3 preceding financial years is negative.

Based on the above, NCLT has passed an order stating that (1) Company is liable to spend the amount on account of CSR for FY 2014-15 taking into account only the net profit before tax for the FY 2013-14. (2) Company to adhere to the other provisions of section 135 of CA13. (3) The Company is permitted to file an application for revision of financial statement or the Board's report after incorporating the information regards CSR for FY 2014-15.

In the current application, the appellant prayed for the following relief:

1. The impugned order of NCLT be quashed.
2. The appellant company is not attracted by the provision of section 135(1) for the FY 2014-15.
3. Average net profit for the purpose of Section 135(5) shall be calculated considering the net profit of all 3 (three) preceding years and
4. Since, the average net profit of last 3 (three) preceding years is negative, the Company is not required to appropriate any amount for CSR in the year 2014-15.

The submission made by the appellant are as follows.

1. It has suffered losses in earlier two financial years for 2011-12 and 2012-13.
2. It has made a net profit before tax of INR 5 crore and after tax is less than ₹ 5 crore.
3. As per section 135, one of the criteria is net profit of INR 5 crores or more during the immediately preceding financial year.
4. If it covered under section 135(1), then only it has to constitute a CSR Committee, spend 2% of average net profit and state the CSR Policy in Board report.
5. As per section 135(1) read with Rule 2(f) of the CSR Rules, 2014, threshold limit is "net profit after tax" and hence company is not attracted by CSR provisions and therefore it did not constitute the CSR Committee and reported in Board Report.
6. Even, if section 135(1) is attracted, the average net profit for 3 preceding years is negative and hence not required to spend 2% on CSR.
7. The amendment to the explanation was made in 2018. Prior to 2018, there was no method for calculating net profit except Rule 2(f) and that is net profit after tax.

The RoC has made the following submission.

1. The FAQ by the Ministry of Corporate Affairs ("MCA") dated 12-1-2016 clarified that calculation of net profit is as per section 198 of CA13, which is primarily before tax. In this case, by above calculation, it has profit of more than INR 5 crore.
2. It disagreed with the appellant's view that even if 135(1) attracts, it doesn't attract section 135(5) provisions for spending, since the average net profit is negative.
3. The amendment to the original explanation is more for clarification. Section 198(5)

clearly provides that while calculating net profit, the income tax and super tax payable shall not be deducted.

4. The method for calculating net profit is applicable to section 135(5) as well as 135(1).

Judgment

The NCLAT has held that the appellant is liable to constitute the CSR Committee as per section 135(1). The method of calculation for section 135(5) would be the same as per formula given and loss should not be deducted twice.

The following points were considered.

1. For considering whether appellant is covered under section 135(1), it has observed that net profit before tax is above INR 5 crore, which appellant also has calculated. This, it is applicable.

2. Due to negative average profit for 3 (three) years, appellant is not required to spend 2%. However, the appellant has not looked at the provisions of section 198(4)(1), which provides the period from when the deduction of excess expenditure over income shall be applicable while computing net profit. Thus, same is permissible only from 2014-15 onwards only. Thus, appellant has deducted the excess of expenditure over income for 2012, 2013 from the net profit of 2014 is not valid under CA13.

3. NCLT's direction to spend the CSR amount only on considering 2013-14 profit is rejected. As per NCLAT, the NCLT's observation is against the mandate of law, which provides for spending 2% of average of last 3 (three) years net profit as CSR. BY NCLT logic, company will never be covered under the average net profit of 3 (three) preceding years.

4. The appellant, while calculating net profit, the figures for 2012 and 2013 have been deducted twice from 2013-14 and hence negative figure.

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True civilization does not mean congregating in cities and living a foolish life, but going Godward, controlling the senses, and thus becoming the ruler in this house of the self.

– *Swami Vivekananda*

Stick to truth and we shall succeed, maybe slowly, but surely.

– *Swami Vivekananda*

Sanjeev Shah and Abdullah Fakih
Company Secretaries

Overview of Companies (Amendment) Act, 2019 – Slew of changes for ease of doing business!

Background

In a major initiative to strengthen the regulatory framework and unclog the burden on National Company Law Tribunal (NCLT), the Government of India (GOI) had on 2nd November, 2018, promulgated the Companies (Amendment) Ordinance, 2018 (Ordinance) and amended the Companies Act, 2013 (Companies Act). However, the Ordinance lapsed and it was reintroduced as Companies (Amendment) Ordinance, 2019 on 12th January, 2019 and as Companies (Amendment) Second Ordinance, 2019 on 21st February, 2019.

To regularise the Ordinance, the Companies (Amendment) Bill, 2019 had been introduced in Parliament. The Companies (Amendment) Bill, 2019 has been passed by the Lok Sabha on 26th July, 2019 and by Rajya Sabha on 30th July, 2019 and the same has received an assent of the President and notified in the *Official Gazette* on 31st July, 2019 (Amendment Act, 2019).

Amendment Act 2019 is a step further to promote ease of doing business, declogging of NCLT and Special Courts. It also clarifies the mandatory requirement relating to spend towards CSR. It also contains provisions that are considered necessary for ensuring more accountability and improved enforcement to strengthen corporate governance norms and compliance management in the corporate sector.

This article contains salient features of the Amendment Act, 2019.

Following provisions of the Amendment Act 2019 shall be effective from 2nd November, 2018

I. Revamping penalties

Certain offences have been recategorised as defaults carrying civil liabilities to bring them under an in-house adjudication mechanism. This has been done in a two-fold manner, i.e. by removal of imprisonment for certain procedural defaults on one hand, and replacing the provision of fine with a penalty, on the other hand.

Removal of imprisonment provision for certain defaults

- Section 53(3) – Issue of shares at a discount
- Section 92(5) – Annual return
- Section 137(3) – Filing of Financial statement with ROC
- Section 64(2) – Alteration of share capital
- Section 159 – Punishment for Contravention in respect of DIN

Fine replaced with penalty for continuing failure

- Section 102(5) – Statement to be annexed to notice of general meeting
- Section 105(3) – Proxies
- Section 117(2) – Resolutions and Agreements to be filed with Registrar of Companies (RoC)
- Section 121(3) – Report on annual general meeting to be filed by listed companies with RoC
- Section 140(3) – Removal, resignation of auditor
- Section 157(2) – Company to inform Director Identification Number (DIN) to ROC
- Section 165(6) – Cap on number of directorships in a company
- Section 191(5) – Payment to Director for Loss of Office, etc., in connection with transfer of undertaking, property or shares
- Section 197(15) – Overall maximum managerial remuneration and managerial remuneration in case of absence or inadequacy of profits
- Section 203(5) – Appointment of Key Managerial Personnel (KMP)
- Section 238(3) – Registration of the offer of scheme involving transfer of shares

II. Ensuring regularization of the default and prescribing stiffer penalties in case of repeated defaults

Towards this end, following changes are made:

Sr. No.	*Section of 2013 Act*	*Particulars*	*Amendment*
1.	454(3) Adjudication of Penalties	Order of adjudicating officer	The adjudicating officer shall in addition to imposing the penalty on the company/the officer in default/any other person, also give the direction of making good the default.
2.	454(8) Adjudication of Penalties	Default in compliance of adjudicating officer's order	Default is deemed to occur not only when the company or the officer in default does not pay the penalty imposed by the order of the adjudicating officer or Regional Director (RD), but also in case of failure to comply with such order.
3.	454A	Penalty for repeated default	Where a penalty in relation to a default has been imposed on a company or any other person, and such company or person commits the same default again within a period of 3 years from the date of order imposing such penalty, passed by the adjudicating officer/RD as the case may be, such company or other person shall be liable for the second and every subsequent defaults for an amount equal to twice the amount provided for such default under the relevant provision of the 2013 Act.

III. Declogging the NCLT

The NCLT has been unburdened in terms of matters that require their approval, some of which have now been moved to Central Government (powers delegated to the Regional Directors [RD]):

a) ***Change in the financial year***

Under section 2(41) of the 2013 Act, Indian companies/foreign companies registered in India are required to follow the period of April–March, as their financial year. However, an Indian company/body corporate which is a holding company or a subsidiary or associate company of a company incorporated outside India, and is required to follow a different financial year for consolidation of its accounts outside India, it is allowed to change the financial year (to a period other than April–March), with the approval of NCLT. The Amendment Act 2019 has transferred the authority of giving approval from NCLT to RD.

b) ***Conversion of public companies into private companies***

In terms of Section 14(1), the power to approve conversion of a public company into a private limited company has been shifted from NCLT to RD.

c) ***Enhancing the pecuniary limits up to which Regional Directors can compound offences***

RD can compound an offence which is punishable with maximum fine of up to ₹ 25 lakh (earlier ₹ 5 lakh).

IV. Declaration for Commencement of business

A company incorporated after 2nd November, 2018 and having share capital cannot commence any business (or) exercise any borrowing powers unless:

a) A declaration is filed by a director with the Registrar of Companies (RoC) within 180 days from the date of incorporation with regard to the receipt of subscription money from each of the subscribers to the memorandum;

b) The company has filed with the RoC within 30 days of incorporation, a verification of its registered office.

If aforesaid declaration of receipt of subscription money is not filed within 180 days of incorporation and the RoC has reasonable cause to believe that the company is not carrying on any business or operations, the RoC is empowered to initiate action to remove the name of the company from the register of companies.

The above provisions are applicable to all companies, whether private or public, having share capital.

V. Non-maintenance of registered office to be a ground for removal of the name of the company

If the RoC has reason to believe that a company is not carrying on any business or operations, it may physically verify the registered office address of the company and if any default is found in complying with the requirement of maintenance of registered office, it may initiate action for the removal of name of the company from the register of companies.

VI. Registration and modification of charges

Maximum time for creation and modification of charge on or after 2nd November, 2018 with RoC has been reduced from 300 days to 60 days from date of creation/modification. In case of delay beyond 60 days, RoC may allow registration within further period of 60 days on payment of *ad valorem* fees.

Central Government has been empowered to extend time or allow rectification, if it is satisfied that the omission to give intimation to RoC for the payment/satisfaction of charges or modification was accidental/inadvertent.

Following provisions shall be effective from a date to be notified by the Central Government (notification awaited):

I. Corporate Social Responsibility (CSR)

- Clarificatory amendment has been made specifying that CSR is also to be undertaken by companies which have not completed 3 financial years since incorporation.
- Unspent amount of CSR spend on any 'ongoing project' fulfilling prescribed conditions will have to be transferred to an 'Unspent Corporate Social Responsibility account' in a scheduled bank within 30 days from the end of the financial year and such amount must be spent on CSR obligation within a period of 3 financial years from the date of transfer. If the money has not been so spent, the amount should be transferred to any of the following funds at the discretion of the Company viz., Swachh Bharat Kosh or Clean Ganga Fund or Prime Minister's National Relief Fund.
- Unspent amount of CSR spend (other than for 'ongoing projects') will have to be transferred to the aforesaid funds within a period of 6 months from the end of financial year.
- Clear shift from "comply or explain" to "compulsory spend". In this regard, penal provisions have been introduced for not spending or shortfall in spending towards CSR viz., the company shall be punishable with fine of at least ₹ 50,000 which may extend to ₹ 25 lakh, and every officer of such company who is in default shall be punishable with imprisonment for a term which may extend to three years or with a fine of at least ₹ 50,000 which may extend to ₹ 5 lakh or with both.
- Central Government has been empowered to give general or special directions to a company or class of companies to ensure compliance of CSR provisions by such companies.

II. Issue of securities in dematerialised form

Currently, public companies are required to issue and transfer securities only in dematerialised form. Now, the Central Government has been empowered to prescribe class of unlisted companies whose securities shall be held and transferred only in dematerialised form.

III. Significant beneficial owner (SBO)

Duty is cast on companies to find out if there is any individual who is a significant beneficial owner in relation to the company. Such individual will be required to comply with the SBO provisions.

IV. National Financial Reporting Authority (NFRA)

a. NFRA shall perform its functions through divisions which will be prescribed by way of Rules, and each such division of NFRA will be presided over by a Chairperson or a full–time person authorised by the Chairperson.

b. In case of professional or other misconduct by member or a firm of chartered accountants, powers of NFRA have been specified to debar such member or firm of chartered accountants from being appointed as an auditor or internal auditor or performing any valuation etc. for minimum period of 6 months (not exceeding 10 years) as against the current power of prohibiting from engaging in practice of a chartered accountant.

V. Disgorgement of assets, properties, cash in case of corporate frauds

Where the report of the Serious Fraud Investigation Office (SFIO) states that fraud has taken place in a company and due to such fraud any director, key managerial personnel, other officer of the company or any other person or entity, has taken undue advantage or benefit, whether in the form of any asset, property or cash or in any other manner, the Central Government may file an application before the NCLT with regard to disgorgement of undue benefits gained by the director, key managerial personnel, other officer or any other person as a result of such fraud and they shall be personally liable without any limit on liability.

VI. NCLT to decide on 'fit and proper' criteria for management of companies in cases of 'oppression and mismanagement'

- Central Government may refer the matter to NCLT under certain set of circumstances (such as fraud, misfeasance, persistent negligence, default in carrying out obligations and functions under the law, breach of trust etc.) to inquire into such matters and record its decision with regards to whether or not a person is a 'fit and proper' person to hold office of the director or any other office connected with the conduct and management of the Company.
- Where a person has been declared as not a 'fit and proper' person, such person shall not hold office of director or any other office connected with the conduct and management of affairs of any Company for a period of 5 years (unless the Central Government permits with the leave of NCLT) and further shall not be entitled to or paid any compensation for loss of office.

Conclusion

While most of the amendments are aimed at ease of doing business in India, penalty for non-spending/underspending of CSR contribution may evoke concerns amongst industry in general.

Source:

1. Companies (Amendment) Act, 2019 as published in the Gazette of India on 31st July, 2019.

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Wealth goes, beauty vanishes, life flies, powers fly – but the Lord abideth forever.

– *Swami Vivekananda*

OTHER LAWS

FEMA – Update and Analysis

CA Mayur Nayak, CA Natwar Thakrar & CA Pankaj Bhuta

In this article, we have discussed recent amendments to FEMA through Circulars and Notification issued by RBI. In addition some recent compounding orders issued by RBI are also discussed.

A. Updated Through AP Dir Circulars

1. External Commercial Borrowings (ECB) Policy – Rationalisation of end-use Provisions

Hitherto, under paragraphs 2.1.(v) and 2.1.(viii) of Master Direction No. 5 dated March 26, 2019, ECB proceeds were not allowed to be utilised for working capital purposes, general corporate purposes and repayment of Rupee loans except when the ECB was availed from foreign equity holder for a minimum average maturity period of 5 years. Further, on-lending for these activities out of ECB proceeds was also prohibited.

In further liberalization of the ECB framework, subject to paragraph 2.2 of the Master Direction 5 *ibid*, RBI has relaxed the end-use restrictions permitting eligible borrowers to raise ECBs for the following purposes from recognised lenders, except foreign branches/overseas subsidiaries of Indian banks-

- ECBs with a minimum average maturity period of 10 years for working capital purposes and general corporate purposes are now allowed. Borrowing by NBFCs for the above maturity for on lending for the above purposes is also permitted.
- ECBs with a minimum average maturity period of 7 years can be availed by eligible borrowers for repayment of Rupee loans availed domestically for capital expenditure as also by NBFCs for on-lending for the same purpose. For repayment of Rupee loans availed domestically for purposes other than capital expenditure and for on-lending by NBFCs for the same, the minimum average maturity period of the ECB is required to be 10 years.
- Eligible corporate borrowers are permitted to raise ECB for repayment of Rupee loans availed domestically for capital expenditure in manufacturing and infrastructure sector classified as SMA-2 or NPA, under any one time settlement with lenders. Lender banks are also permitted to sell, through assignment, such loans to eligible ECB lenders, except foreign branches/overseas subsidiaries of Indian banks, provided, the resultant external commercial borrowing

complies with all-in-cost, minimum average maturity period and other relevant norms of the ECB framework.

RBI has clarified that the prescribed minimum average maturity provision, as above, for the aforesaid end-uses will have to be strictly complied with under all circumstances.

(***Source**: AP Dir. Series Circular No. 4 dated 30th July, 2019*)

(***Comment***: **Relaxation in ECB norms brought by RBI in consultation with Government of India is an important step taken in order to address current unprecedented liquidity crunch experienced by Indian economy caused due to global and domestic factors. It offers opportunity to eligible borrowers to raise cheap foreign currency funds for working capital/general corporate purposes. It also allows NBFCs to raise funds for on lending for the permitted maturity and end uses. RBI move also allows manufacturing and infrastructure companies classified as SMA-2 borrowers (who have delayed payments beyond 60 days but remain under 90 days cutoff for NPAs) or NPAs to avail ECB for settling their existing capital expenditure Rupee loans with local banks under any one time settlement arrangement. It could help banks to reduce their stress. With lack of greenfield projects coming up, foreign funds could move to hunt valued stressed assets which could fetch them a higher yield than LIBOR plus 450 basis points. Thus it helps both local lenders as well as corporates to spruce up their financials. This move in the long run has great potential to result into win-win situation for Indian economy, corporate, banks & the foreign lenders**.)

B. Updated Through Notifications

1. Amendment in Notification No. FEMA 5(R) Foreign Exchange Management (Deposit) Regulations

- Sub-regulation 3 of regulation 6 including all the words and expression contained therein shall be deleted which allowed Indian companies to accept deposits by issue of Commercial Paper to a non-resident Indian or a person of Indian origin or a foreign portfolio investor registered with the Securities and Exchange Board of India subject to certain conditions.

(***Source**: Foreign Exchange Management (Deposit) (Amendment) Regulations, 2019 vide GSR No. 498(E) dated 16.07.2019/FEMA 5(R)2/2019-RB dated 16.07.2019*)

C. We have discussed below few recent compounding order issued by RBI

1. Transfer or Issue of Security by a Person Resident Outside India (Inbound Investment) (FEMA 20/2000-RB)

1) Delay in reporting the transfer of shares from Resident to Non-Resident investors

Applicant	M/s British Orient Infotel Private Limited
Compounding Application Number	C.A. No. BGL 382/2019

Compounding Authority Name	Foreign Exchange Department, Bengaluru
Amount imposed under Compounding Order	₹ 1,20,124/-
Date of order	18th June, 2019
Facts of the case	A resident shareholder of the applicant company had transferred equity shares held by him in the applicant company to a Non-Resident, M/s Dictate IT Limited, UK on 18th February 2009. The form FCTRS was filed on 05th December 2018.
Selected Contravention	***Delay in submission of form FC-TRS on transfer of shares from Resident to Non-Resident:*** Paragraph 10A(b)(i) of r.w. paragraph 10 of schedule 1 to Notification No. FEMA 20/2000-RB provides that in case of transfer of shares or convertible debentures of an Indian company by way of sale from a person resident in India to a person resident outside India or vice versa, the transferor/transferee, resident in India, shall submit to the AD bank a report in the form FC-TRS specified by Reserve Bank from time to time, within 60 days from the date of receipt or payment of the amount of consideration. The onus of submission of the form FC-TRS within the specified time shall be on the transferor/transferee resident in India.
Comments	Regulation 13.1 (4) of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Regulation 10A(b)(i) of erstwhile FEMA 20/2000- RB dated May 3, 2000. The application has been compounded for non-filing of Form FC-TRS resulting into violation of Reg. 10(A)(b)(i). This is in addition to violation of Reg. 4 for taking transfer on record transfer without prior approval of RBI for which he is penalized.

2) Transfer or Issue of any Foreign Security (Outbound Investment) (FEMA 120/2004-RB)

Repatriation of the disinvestment proceeds beyond the stipulated period of 90 days

Applicant	Standard Greases & Specialities Pvt. Ltd.
Compounding Application Number	C.A. No. 4893/2019
Compounding Authority Name	Foreign Exchange Department, Mumbai

Amount imposed under Compounding Order	₹ 59,036/-
Date of order	12th June, 2019
Facts of the case	The applicant had made an equity contribution in overseas JV viz. Standard Greases and Specialities LLC, UAE. Subsequently, the applicant entered into an agreement dated 10th July 2017 to disinvest stake in overseas JV to a NR *viz.* Khaleej Lubricants and Specialities FZE, UAE. The sale consideration was received on 18th December 2017, but it was received from the Gulf Oil Middle East Limited, UAE-parent company of the acquirer viz. Khaleej Lubricants and Specialities FZE. The AD bank advised the applicant to bring sale consideration from the acquirer only. Accordingly, the amount was returned to Gulf Oil and payment was received from Khaleej Lubricants and Specialities FZE on April 16, 2018.
Contravention	***Repatriation of the disinvestment proceeds beyond the stipulated period of 90 days:*** Regulation 16(2) of Notification No. FEMA 120/2004-RB requires sale proceeds of shares/securities to be repatriated to India immediately on receipt thereof and in any case not later than 90 days from the date of sale of the shares/securities through the designated authorized dealer. As the applicant received disinvestment proceeds beyond the stipulated time period of 90 days, it resulted in contravention of Regulation 16(2).

3) Acquisition and Transfer of Immovable Property in India (FEMA 21/2000-RB)

Acquisition of immovable property by non-resident foreign national in India without RBI permission

Applicant	Mr. Joel Queirel and Mrs. Benedicte Pascale Mireille Caille
Compounding Application Number	C.A. No. 90/2019
Compounding Authority Name	Foreign Exchange Department, New Delhi
Amount imposed under Compounding Order	₹ 30,00,000/-
Date of order	26th February, 2019

Facts of the case	The applicants, both being non-resident, foreign citizens of non-Indian origin had acquired a plot in Kerala, India by way of purchase in joint names and subsequently built a residential building on the same plot. The cost of acquisition of the land was ₹ 15,00,000/- and cost incurred for construction was ₹ 85,00,000/-.
	The applicants were advised by the RBI to sell the property under reference to a person resident in India within 6 months. The applicant sold the said property to a company incorporated in India for ₹ 75,00,000/-. The applicants submitted the valuation report valuing the land and building at ₹ 84,91,000/-. However, RBI independently obtained valuation report wherein the land and building were valued at ₹ 1,28,75,000/-. The purchase price of the immovable property under reference *viz.* ₹ 15,00,000/- and construction cost of building *viz.* ₹ 85,00,000/- aggregating to ₹ 1,00,00,000/- were considered as the amount of contravention. Undue gain is calculated by RBI based on independent valuation report obtained by the RBI.
Contravention	***Acquisition of immovable property by non-resident being foreign national in India without RBI permission:*** Regulation 8 of Notification No. FEMA 21/2000-RB states that "save as otherwise provided in the Act or Regulations, no person resident outside India shall transfer any immovable property in India, provided that the Reserve Bank may, for sufficient reasons, permit the transfer, subject to such conditions as may be considered necessary.." In this case, applicants being non-resident – foreign citizen of non-Indian origin had acquired the immovable property in India without the prior approval of the RBI. Thus, the applicants contravened the provision of Regulation 8.
Comments	Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2000 has been replaced by revised regulations; Regulation 10 of extant FEMA 21(R)/2018-RB dated 26-3-2018 corresponds to Regulation 8 of erstwhile FEMA 21/2000- RB dated 3-5-2000.

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CA Prashant Daftary & CA Rakesh Jain

Reality check for Real Estate Companies: Revenue recognition under Ind AS 115

Background

Real estate industry has been in a constant state of turmoil since last few years and has been severely impacted by demonetization, RERA, GST and other factors like liquidity issues, low demand etc. In addition to these factors, the real estate companies (especially the large companies and listed companies) have also been impacted by transition to Ind AS (which are in line with IFRS). This transition involved changing from earlier accounting standards to Ind AS. One of the change that had the most significant impact was with respect to the revenue recognition. Revenue recognition in real estate is more peculiar as compared to many other industries on account of following factors:

- Project duration ranging from 3-5 years
- Significant reliance on management judgment and assumptions as regards to cost and expected project profitability
- Practices and peculiarities in different states
- External factors like approvals from government authorities, local bodies etc.

In this write-up, we have analysed how this transition has affected the financial statements, various position taken up by different companies and how an investor/lender should read the financial statements of the real estate companies.

Implementation of Ind AS 115

Upon transition to Ind AS, the specified class of real estate companies were required to comply with Ind AS 18 – 'Revenue' and Guidance Note on Accounting For Real Estate Transactions issued by the ICAI up to FY 2017-18. With effect from 1st April 2018, the companies are required to adopt Ind AS 115 – 'Revenue from Contracts with Customers'. This effectively meant two levels of transition and thus making the entire process very complex.

Prior to Ind AS, the real estate companies were following the requirements of Accounting Standard - 9 on "Revenue Recognition" and the Guidance Note on Real Estate issued by the ICAI. Based on the same, revenue was generally being recognized on percentage of completion method. The guidance note provided guidelines as regards computation of percentage of work completion and how revenue should be recognized. This guidance note broadly ensured consistency in the method of accounting and was also being generally accepted by the tax authorities.

Post Ind AS 115, 5 step model needs to be followed for revenue recognition as given below:

Step 1 : Identify the contract(s) with the customer

Step 2 : Identify the separate performance obligations in the contract

Step 3 : Determine the transaction price

Step 4 : Allocate the transaction price to the performance obligations

Step 5 : Recognise revenue when (or as) each performance obligation is satisfied

The key factor in the above conditions is 'satisfaction of performance obligation', as this determines whether revenue can be recognised 'at a point of time' or 'over a period of time'. In case of real estate, customer enters into an agreement with the developer (generally at construction stage) whereby the customer agrees to make payments based on specified milestones or other terms and in return developer promises to handover the property (flat, apartment etc.) along with the agreed amenities as per the agreed time-line. Here a judgement is required to be made whether performance obligation is satisfied over a period of time or at a point of time.

If we conclude that the performance obligation is satisfied over a period of time then revenue recognition on percentage of work completed ('POCM') is possible and in other cases, revenue can be recognized only upon completion of work ('Completed Contract').

POCM vs. Completed Contract

Revenue recognition by real estate sector under Ind AS 115 was a subject matter of major controversy. There were multiple articles and newspaper reports which expressed a view that it would no longer be possible for real estate companies to take up a position that obligations are satisfied 'over a period of time' and all companies would have to change from POCM to Completed Contract which would have significant impact on the financial statements.

The ICAI cleared this misconception by issuing a clarification. This clarification stated that the Ind AS 115 does allow recognition of revenue using POCM and has explicit and specific requirements to recognise revenue, where performance obligation is satisfied over a period of time. It may be noted that paragraphs 35-37 of Ind AS 115 explicitly permit recognition of revenue using POCM, where the performance obligation is satisfied over time. The clarification further stated that the recognition of revenue on POCM is possible based on prevalent long established legal system/jurisprudence in India, and facts and circumstances of individual case/contract.

Based on above, it is clear that both methods of revenue recognition are possible depending upon the terms of the contract and compliance with specific requirements of the standard. Some of the key points that needs to be considered while making the above judgement are as under:

- **Cancellation clause**: Ability of customer to cancel the contract without a default by the developer
- **Restrictive clauses:** Whether the agreement restricts the customer from selling or transferring the property which is under construction or whether the selling price in such a situation is controlled by the developer
- **Historical trend:** History of cancellation/ actual trade practice followed by the developer
- **Actionable claim over dues:** Whether the developer has an enforceable right to payment
- **Nature of arrangement**: Whether the arrangement is in substance a financing arrangement

Other areas with divergent views affecting revenue recognition

- ***Minimum threshold of revenue recognition***
  In case of companies which recognize revenue based on POCM, there is no bright line test (as compared to guidance note on real estate under Ind AS-18) for minimum threshold of construction, area sold and collection. Consequently, different companies would apply different principles & judgements.

  Further, as under Ind AS 115, a company can recognize revenue equal to the cost in case where minimum threshold limit is not achieved. This was not permitted under previous standard. However, this will have no impact on profit and loss for the period.

- ***Joint development arrangements/barters***
  Real estate developers in India generally enter into various Joint Development agreements (JDA's) with land owners for developing land in return for free of cost constructed area or share of revenue. Developers also enter into redevelopment agreement with societies owners for demolition and reconstruction of the existing buildings. Developer gets development rights by way of built-up area.

  In such arrangements, identifying customer under Ind AS 115 would require judgment and based on the nature of arrangement, the accounting treatment could undergo a change. In case of an arrangement in the nature of revenue share, the landowner may not be considered a customer whereas in case of arrangement to share a specified built-up area, the landowner would be considered as a customer and accordingly accounting treatment would differ.

- ***Slum rehabilitation***
  In case of slum rehabilitation project, where the company constructs free of cost area (rehab building) in return of specified Floor Space Index (FSI), whether the government or relevant authority would be considered as a customer or not would require a careful consideration.

Ind AS 115 vs. Income-tax vs. GST

Another aspect where special attention would be required is what method of revenue recognition is acceptable to the tax authorities. Following key factors needed to be considered:

- ***Income Tax***
  - Income tax department is expected to come out with Income Computation and Disclosure Standard (ICDS) for Real Estate Sectors. As per draft ICDS, revenue recognition would be required as per POCM and hence for some companies this would mean virtually keeping two separate set of books of account and multiple reconciliations to satisfy the tax authorities and various stakeholders.

    Further, companies, which have shifted from POCM to completed contract on transition need to keep track of revenue/profit already offered for tax in earlier years and income taxes paid thereon.
  - Presently under minimum alternate tax there is no specific exemption/adjustment for transition adjustments under Ind AS 115 and hence it is possible that same revenue may be taxed twice (especially relevant for companies falling under MAT).

- ***GST***
  - Goods and Services Tax (GST) is collected and paid based on demand raised on customers on accrual basis and hence reconciliation of book of accounts with GST returns will be an enormous task.

Accounting policy adopted by leading Real Estate developers

Based on the analysis of method applied for revenue recognition by 20 large listed entities, majority of companies have shifted from POCM to Completed Contract except two companies. Transition to Ind AS 115 has had a significant impact on the net worth of these listed companies; however, this impact would be temporary and is more of a timing difference.

Investors/lenders perspective – Tips to analyse the financial statements

From investor/lenders perspective, the application of Ind AS 115 by real estate sector can be confusing (especially for retail investors) and would be difficult in understanding/projecting the revenue/profit numbers on account of the changes in accounting policies and varied practices followed. Some key points, which need to be considered by investor/lenders for reviewing financial statements of real estate entity:

- **Non-comparability with previous year:** Financial numbers for FY 2018-19 would not be fully comparable with the earlier year numbers on account of this change. Companies that have adopted completed contract method have reversed the revenue recognized in earlier years and would once again recognize the revenue when the project is completed. This would lead to recognition of revenue of same project twice (adjustment on transition has done through retained earnings, though option of revising previous year financials is available).
- **Benchmarking:** It would not be possible to benchmark real estate companies following different methods of revenue recognition based on declared revenue, profit numbers and inventory levels. Analysis based on Earnings Per Share/Price Earning ratio would also be misleading.
- **Security coverage:** Lenders while determining the inventory and receivables for the purpose of security/drawing power would need to have a better understanding of method of revenue recognition and stage of completion of work. As this would have a consequential impact on the inventory/ work in progress.

In order to give a better understanding and comfort to the investors/lenders, the real estate companies would have to suitably explain how the transition has impacted them in terms of past and also how would this impact them going forward.

Conclusion – need for guidance (which is missing)

Considering the multiple practices followed by different real estate companies and different requirements under various tax laws, there is definitely a need for an overall/comprehensive review of various practices, to come out with a common methodology to facilitate ease of doing business, better benchmarking and consistency among the industry. Guidance Note for Real Estate Developer by the ICAI would be much appreciated to clarify on the above issues.

BEST OF THE REST

Rahul Sarda,
Advocate

Property inherited from father by sons – Is it joint family property in the hands of sons? Can it be alienated without consent of grandsons?

The brief facts of the case are that Shri Chikkanna (since deceased) was the propositus of the joint family. He had three sons, namely, Pillappa, Venkataramanappa and Muniyappa (Respondent Nos. 7, 8 and 9). Respondent nos. 1 to 4 and Respondent No. 10 are the sons of Pillappa (defendant No. 2) and Respondent Nos. 5 and 6 are the sons of Shri Venkataramanappa (defendant No. 3).

Chikkanna purchased the suit property in question from his sister Thayamma. The sons i.e., Pillappa, Venkataramanappa and Muniyappa sold the suit property to Muthappa under a sale deed dated 2-12-1950. It was stipulated in the sale deed that in the event of the sale of the suit property by the above named Muthappa, the suit property shall be reconveyanced in favour of Pillappa, Venkataramanappa and Muniyappa at the price offered by the purchaser and on their failure, the above named Muthappa would be free to sell the suit property to any other purchaser. The property was later purchased under the sale deed dated 30-9-1954 by one Muniswamy @ Annaiyappa from whom Doddamuniyappa purchased the suit property under the registered sale deed dated 29-1-1962.

Pillappa, Venkataramanappa and Muniyappa i.e. sons of Chikkanna filed a suit on 27-6-1964 against Doddamuniyappa including other Defendants seeking decree of reconveyance of the property in terms of the clause of reconveyance and directing the Defendants in the suit to execute reconveyance deed in their favour in respect of the suit property which came to be dismissed by the trial Court. The appeal was allowed and the suit was decreed and confirmed in second appeal.

During execution proceedings, Muniyappa, with the knowledge of his two brothers i.e. Pillappa and Venkataramanappa entered into a compromise dated 25-3-1976 with Doddamuniyappa whereunder Doddamuniyappa would be the owner of a portion of the suit property. In terms of the compromise, the part premises was handed over to Doddamuniyappa.

The Respondents had inherited the property from their late father i.e. propositus. They sold the same to one purchaser. The sale deed contained clause of reconveyance of the property in favour of the respondents. The said purchaser without reconveyancing sold the property to the Appellant. The Respondents filed a suit wherein the deed of reconveyance was executed and possession of the property was delivered to them. The Appellant filed an execution application and a compromise was executed wherein part of possession of the property was restored to the Appellant.

The grandsons of Chikkanna, after attaining majority, filed a suit for declaration that the said compromise decree was not binding on them and for permanent injunction contending *inter alia* that the said compromise had been entered into without their knowledge and consent and that Pillappa, Venkataramanappa and Muniyappa did not have any right whatsoever to enter into compromise.

The trial Court dismissed the suit holding that the plaintiffs i.e., grandsons of Chikkanna failed to establish that it was the joint family property in the hands of Pillappa, Venkataramanappa and Muniyappa (which they could not have dealt with) and held that Pillappa, Venkataramanappa and Muniyappa were the joint owners of the suit property. The High Court allowed the appeal and decreed the suit.

Held by the Supreme Court that when the possession was restored the property resumed its original character of joint family in the hands of the respondents and this the subject property was joint family property in the hands of Pillappa, Venkataramanappa and Muniyappa. This created a right of inheritance in the grandsons of Chikkanna for whom the subject property would be ancestral property and who were neither consulted nor made parties to the said compromise. Therefore, the compromise cannot bind them but only Pillappa, Venkataramanappa and Muniyappa who were parties to the compromise.

Doddamuniyappa (Dead) through LRS. vs. Muniswamy & Ors., Civil Appeal No(s).7141 of 2008 dated 01/07/2019, Supreme Court

When does the relinquishment of claim bar the second suit – Principles of Order II, Rule 2 – Pleadings of both suits to be seen

The owner of a piece of land sold a part of the said land and a sale deed to that extent was executed and entered into between him and the purchaser. Similarly, after sometime the balance portion of the land was also sold to the same purchaser and a sale deed was executed and entered into between them. The family members of the said owner filed a suit in the Trial Court praying for setting aside the first sale deed. However, the Trial Court dismissed the suit by stating that the owner had a rightful title and that the purchaser by virtue of the said sale deed was the rightful owner of the property and the sale was a valid.

The family members once again filed a suit with the same prayer in respect of the second sale deed. The Trial Court and the first appellate court dismissed the said suit by stating that the suit was barred by Order II Rule 2 of CPC and constructive *res judicata.* According to the Court, the second alienation ought to have been subject matter of the earlier suit. On appeal before the High Court, the order of the Trial Court was reversed by holding that there was separate cause of actions and constructive *res judicata* will not apply. Being aggrieved by the said reversal purchaser challenged the order of the High Court.

It was submitted on behalf of the Appellant that the cause of action in the first suit is identical with that of the second suit and on the date of institution of the first suit the second alienation was available to be impugned and hence Order II, Rule 2 barred the institution of the second suit.

The family members submitted that the cause of action in both the suit was different and attention of the Court was drawn to

Order VII, Rule 1 and to Article 109 of the Limitation Act. According to him, the period of limitation of the second sale deed is different from that of the first sale deed.

The question before the Supreme Court was whether the High Court was right in holding that the bar of Order II, Rule 2 will not apply. The Court referred to the pleadings of the two suits which were substantially the same. The Court referred to various previous decisions of the Court and that of the privy council wherein the test of cases falling under Order II, Rule 2 were elucidated. Order II, Rule 2(1) provides that a plaintiff is to include the whole of the claim, which he is entitled to make, in respect of the cause of action. However, it is open to him to relinquish any portion of the claim. Order II, Rule 2 provides for the consequences of relinquishment of a part of a claim and also the consequences of omitting a part of the claim. It declares that if a plaintiff omits to sue or relinquishes intentionally any portion of his claim, he shall be barred from suing on that portion so omitted or relinquished. The Court relied upon "Cause of action", as explained by the Privy Council in *Mohammad Khalil Khan* case, meaning the media through which the Plaintiff seeks to persuade the Court to grant him relief. It could, therefore, be said to be the factual and legal basis or premised upon which the Court is invited by the Plaintiff to decide the case in his favour. As regards the plea of *res judicata*, the Court held that the plaintiff who is sought to be prevented by the bar of constructive *res judicata* should have notice about the plea and have an opportunity to put forth his contentions against the same. In the present case, there was no plea of constructive *res judicata*, nor did the appellant-plaintiff get opportunity to meet the case based on such plea. *Res judicata* means "a thing adjudicated", that is, an issue that is finally settled by judicial decision.

All claims and reliefs, which arise from a cause of action, must be comprehended in one single suit. Order II, Rule 2 provides for the principle of repose. If this be the underlying object of Order II, Rule 2, the fact that at the time when the first suit was filed even though the second alienation could be challenged and it stemmed from one single cause of action and not two different causes of action, the mere fact that a different period of limitation is provided, cannot stand in the way of the bar under Order II, Rule 2. The Court held that bar under Order II, Rule 2 would apply. The Appeal was allowed and the judgment of the High Court was set aside.

Pramod Kumar & Anr vs. Zalak Singh & Ors., Civil Appeal No. 1055 of 2019 dated 10/05/2019, Supreme Court

Whether a gift deed registered after death of the donor is valid?

The original owner of the suit property passed away and the property was inherited by his wife. Prior to her death, she through a gift deed gifted the suit property to her grandsons i.e. the Appellants. The Respondents raised strong doubt as to the legality and validity of the said deed.

The Respondents had filed a suit before the Trial Court stating that the Appellants in collusion with some questionable persons had manufactured the said deed in respect of the suit property. According to him, on the date of execution of the said deed, the donor had no sense and capacity to execute the said deed. The suit filed was dismissed by the Trial Court. The Respondents then challenged it before the First Appellate Court. The suit was decreed in favour of the Respondents. The Appellants challenged the legality and validity of the judgment and decree of reversal by the First Appellate Court.

The Advocate for the Appellant argued that the respondents made out a case to the effect that the deed of gift in question was not executed by donor. However, in cross-examination, the respondent stated that the donor used to stay under the care of the Appellants. It was submitted that the respondents failed to produce any evidence in support of their pleading and secondly, evidence of respondent's witness to the effect that the Appellants got the deed of gift executed by undue influence upon the donor was not pleaded by the respondents. Order 6, Rule 4 of the Code of Civil Procedure requires that complete particulars of fraud shall be stated in the pleadings. Hence, the burden of proof lies on the respondents to prove their case. But wrongly the burden of proof was laid on them by the First Appellate Court.

Whereas the arguments advanced by the other side was that the gift deed has been executed by exerting undue influence on the donor. However, the cross examination of the Appellant's witnesses revealed that the donor was physically fit and mentally alert on the date of execution of the said gift deed. If that be the condition, there is no explanation as to what prevented the donor from attending the local registration office and why the gift deed was not registered by donee.

The High Court referred to the definition of "Gift" as defined u/s. 122 of Transfer of Property. It was observed that the deed of gift satisfies the requirement of Section 122 of the Transfer of Property Act read with Section 17 of the Registration Act, there was no scope to say that the said deed of gift is invalid. Section 123 of the Transfer of Property Act stipulates that a deed of immovable property can be made only for transferring the right, title and interest by the donor to the donee by a registered instrument signed by or on behalf of the donor and must be attested by at least two witnesses. The court held that it is a well-established law that it is not necessary for the validity of a deed of gift that it should be registered by the donor himself and relied upon the judgment *Bhabotosh vs. Soleiman* reported in 33 Cal 584. Due execution and attestation of the gift deed by at least two witnesses are required to be proved to admit a deed of gift in evidence. In the instant case, both the execution and attestation of the deed of gift were proved.

It was held that the judgment and decree of First Appellate Court is liable to be set aside and the appeal was allowed.

Dinabandhu Mondal & Ors. vs. Laxmi Rani Mondal & Ors., SA No. 596 of 2008 dated 17/06/2019, Calcutta High Court

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TAX ARTICLES FOR YOUR REFERENCE

Kishor Vanjara,
Tax Consultant

Articles published in Taxman, The Bombay Chartered Accountant Journal (BCAJ), The Chamber's Journal (CJ), The Chartered Accountant Journal (CAJ), All India Federation of Tax Practitioners Journal (AIFTPJ), Goods & Sales Tax Practitioners Association of Maharashtra (GSTPAM), Times of India and Economic Times for the period June 2019 to July 2019 has been arranged and indexed topic-wise.

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THE CHAMBER NEWS


CA Ketan L. Vajani & CA Haresh P. Kenia,
Hon. Jt. Secretaries

Important events and happenings that took place between 4th July, 2019 to 12th August, 2019 are being reported as under:

I. ADMISSION OF NEW MEMBERS

1) The details of new members who were admitted in the Managing Council Meeting held on 4th July, 2019 are as under:–

Type of Membership	**No. of Members**
Ordinary Member	1

II. PAST PROGRAMMES

1. DIRECT TAXES COMMITTEE

Workshop on Direct Tax Provisions of Finance Bill (No. 2), 2019 (jointly with WIRC OF ICAI) was held on 13th July, 2019 at Babubhai Chinai Hall, 2nd Floor, IMC, Churchgate. The workshop was addressed by CA Yogesh Thar and CA N. C. Hegde. CA Kishor Karia was the chairman of the workshop.

III. FUTURE PROGRAMMES

1. ACCOUNTING & AUDITING COMMITTEE

Workshop on Assurances & Compliances is scheduled to be held on 7th September, 2019 at Babubhai Chinai Hall, 2nd Floor, IMC, Churchgate.

2. DIRECT TAXES COMMITTEE

Half Day Workshop on Practical & Legal Issues in Tax Audit is scheduled to be held on 17th August, 2019 at Walchand Hirachand Hall, 4th Floor, IMC, Churchgate.

3. INTERNATIONAL TAXATION COMMITTEE

Full Day Seminar on TDS u/s. 195 on Foreign Remittances including procedural aspects is scheduled to be held on 3rd August, 2019 at West End Hotel, Near Bombay Hospital, New Marine Lines, Churchgate.

4. MEMBERSHIP & PR COMMITTEE

Half Day Seminar on Audit and FEMA at Nashik is scheduled to be held on 7th September, 2019 at The Institute of Engineers Hall, Nashik.

5. STUDENT COMMITTEE

- Workshop on Tax Audit for Students is scheduled to be held on 5th September, 2019 at Babubhai Chinai Hall, 2nd Floor, IMC, Churchgate.
- Interactive Workshop for Students on GST Annual returns and GST Audit is scheduled to be held on 13th August, 2019 at The Mysore Association Auditorium, Conference Room, Matunga.

6. STUDENT COMMITTEE AND MEMBERSHIP & PUBLIC RELATIONS COMMITTEE

The 5th CTC Football Cup is scheduled to be held on 10th August, 2019 at Dr. Antonio Da Silva High School, Dadar West.

7. CHAMBER'S STUDY GROUP AT HYDERABAD (NEW INITIATIVE)

The Chamber of Tax Consultants is pleased to announce formation of a new Study Group at Hyderabad for the benefit of its members in and around Hyderabad City. The purpose of the Study Group is to enable the members to have discussion based learning on variety of topics including Direct Tax, Indirect Tax, International Tax and also Allied Laws. The Study Group will have at least one meeting in a month and will try to cover the topics as per the suggestions from the members based at Hyderabad. The meeting of the Study Group may have one or more speakers/group leaders depending on the subject involved.

Eminent faculties will be leading the discussion for this group. The discussion at the Study Group will focus on various day-to-day issues being faced by the professionals and will cater to the needs of the professionals as may arise from time-to-time.

The Chamber firmly believes that the members at Hyderabad will take the maximum advantage of this new Study Group.

Fees from August 2019 to March, 2020 is ₹ 5200/- + ₹ 936/- (18% GST) = ₹ 6136/-. Interested members can make their payment by DD/Cheque in the favour of "The Chamber of Tax Consultants or visit our website www.ctconline.org for online payment.

The members interested to join the above study group are requested to inform about their willingness to join by sending an e-mail to: office@ctconline.org or message any of the following coordinators:

CA Manindar Kakarla (9700734609)
CA Ram Murthy T. (9848139153)
CA Samba Murthy P. (9490412501)
CA Neelesh Vithlani (9246344232/9494440232)
CA Ravi Ladia (9985722713)

The Meeting for the month of August 2019 will be finalised soon and the details for the same will be informed to the members in due course.

(For details of the future programmes, kindly visit www.ctconline.org or refer The CTC News of August, 2019)

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Residential Refresher Course Committee

Capital Market Study Circle Meeting on "Market Vision & Effects on Economy pursuant to Finance Bill 2019" was held on 12th July, 2019 at Babubhai Chinai Hall, 2nd Floor, IMC, Churchgate

Dignitaries on Dais. Seen from L to R: CA Ankit Sanghvi (Vice-Chairman), CA Mehul Sheth (Chairman), Mr. Nayan Mehta (Speaker), CA Vipul K. Choksi (President), CA Anish M. Thacker (Vice-President) and CA Charu Ved (Member)

Study Circle & Study Group Committee

SC meeting on "Direct Tax Provisions of Finance Bill, 2019" was held on 18th July, 2019 at Babubhai Chinai Hall, 2nd Floor, IMC, Churchgate

Dignitaries on Dais. Seen from L to R: CA Dilip Sanghvi (Co-Chairman), CA Ashok Sharma (Chairman), CA Anish M. Thacker (Vice-President), CA Praful Poladia (Speaker) and CA Dinesh Shah (Convenor)

Direct Taxes Committee

Webinar on "Niceties of Presumptive Taxation – Section 44AD and 44ADA" was held on 13th July, 2019

CA Kalpesh Katira addressing the delegates

ISG on "Recent Important Decisions under Direct Taxes" was held on 22nd July, 2019 at CTC Conference Room.

Mr. Ravi Sawana, Advocate addressing the delegates

Indirect Taxes Committee

IDT SC on "Practical Issues regarding GST Annual Return and GST Audit" was held on 23rd July, 2019 at Jai Hind College, 4th Floor, Churchgate and Webinar was held on 2nd August, 2019 at CTC conference room.

CA Vasant Bhatt addressing the delegates

CA Vikram Mehta addressing the delegates

Membership and PR Committee

Public Meeting on The Union Budget, 2019 was held on 7th July, 2019 at Ghatkopar (Jointly with Forum of Free Enterprise, Ghatkopar CPE Study Circle of WIRC, Ghatkopar Jolly Gymkhana, Investor Education and Welfare Association, Lions Club of Bombay – uptown, Lions Club of Vidhyavihar, Rotary Club of Mumbai – Ghatkopar, GSTPAM and WIRC of ICAI)

International Taxation Committee

Webinar on "Revised Foreign Liabilities and Assets Information Reporting (FLAIR) system and understanding FLA form" was held on 6th July, 2019

CA Vishal Shah addressing the delegates

CTC

Live Screening of The Union Budget, 2019 was held on 5th July, 2019 at CTC Conference Room.

Members at the screening

Birthday wishes to Shri V. H. Patil, Past President by CA Vipul K. Choksi (President) and CA Anish M. Thacker (Vice-President)

Shree Satyanarayana Puja

Shree Satyanarayana Puja was held on 20th July, 2019 at CTC Office.

Membership and PR Committee

Half Day Seminar on GST Annual Return and GST Audit (Form 9 and 9C) was held on 21st July, 2019 at Vishwaisharayya MSEB Hall, Tarabai Park, Kolhapur

CA Manish Gadia addressing the delegates

CA Madar Telang addressing the delegates

Direct Taxes Committee

Half Day Workshop on Direct Tax Provisions of Finance Bill (No. 2), 2019 (Jointly with WIRC of ICAI) was held on 13th July, 2019 at Babubhai Chinai Hall, 2nd Floor, IMC Churchgate

CA Vipul K. Choksi (President) giving his opening remarks

CA Priti Savla (Chairperson – WIRC of ICAI) welcoming the speakers

Faculties

CA Kishor Karia addressing the delegates

CA N. C. Hegde addressing the delegates

CA Yogesh Thar addressing the delegates

International Taxation Committee

Full Day Seminar on TDS u/s. 195 on Foreign Remittances including Procedural Aspects was held on 3rd August, 2019 at Hotel West End, New Marine Line, Churchgate

CA Anish Thacker (Vice-President) giving his opening remarks. Seen from L to R: CA Ronak Doshi (Convenor), CA Rajesh L. Shah (Chairman), CA Vispi Patel (Speaker) and CA Siddharth Parek (Member)

CA Rajesh L. Shah (Chairman) welcoming the speakers

CA Vispi Patel addressing the delegates

CA N. C Hegde addressing the delegates. Seen from L to R: CA Kirit Dedhia (Vice-Chairman), CA Anish Thacker (Vice-President) and CA Ronak Doshi (Convenor)

CA Vishal Gada addressing the delegates

CA Shabbir Motorwala addressing the delegates. Seen from L to R: CA Isha Shekri (Convenor), CA Anish Thacker (Vice-President) and CA Ujwal Thakrar (Member)

CA Vishal Shah addressing the delegates

Brains' Trust Session. Seen from L to R: Shri M. P. Lohia, Ex-IRS (Panelist), CA T. P. Ostwal (Session Chairman) and CA Sushil Lakhani (Panelist)


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