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A Monthly Journal of
The Chamber of Tax Consultants

THE CHAMBER'S JOURNAL

Vol. VII | No. 9 June 2019

YOUR MONTHLY COMPANION ON TAX & ALLIED SUBJECTS

Shares and Securities

PART II

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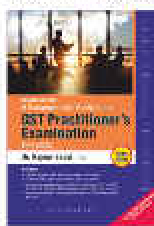

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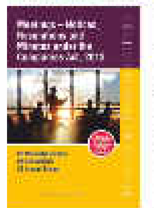

The book aims at providing 'ready to use' drafts as a guide covering all the relevant and updated provisions of the Companies Act, 2013, the rules framed thereunder and the Secretarial Standards issued by the Institute of Company Secretaries of India. Useful for CS, CA, Advocates, entrepreneurs, academicians etc.

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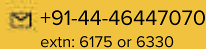

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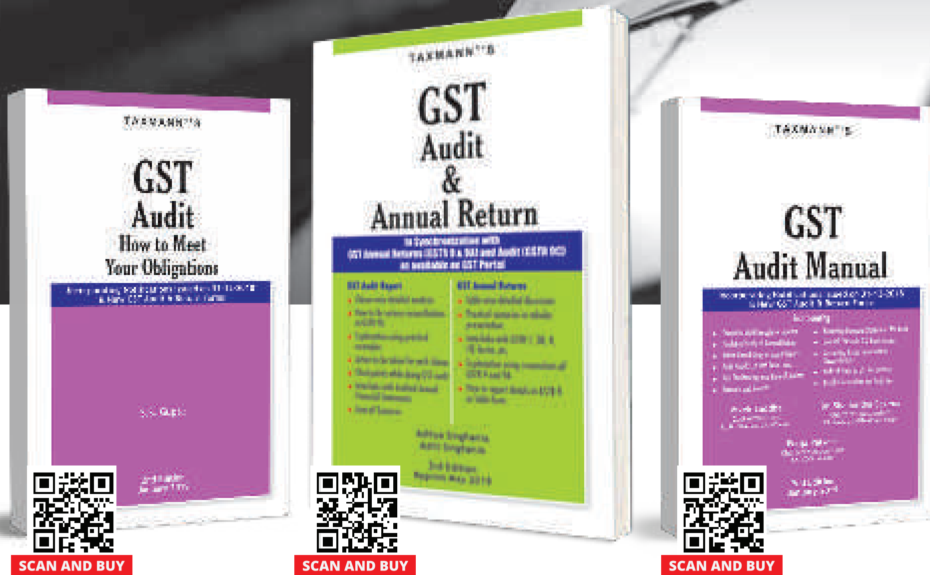

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Editorial

Dear Friends,

Malcom Gladwell, while introducing his book "Outliers, the Story of Success" says "It's not enough to ask what successful people are like… in other words, it's only by asking where they are from that we can unravel the logic behind who succeeds and who doesn't."

This becomes relevant in the present political situation in our country. The outcome of the general Elections has seen that many legacies have been decimated without any trace proving that success is not an issue of bloodline. The three ways to achieve success are hard work, hard work and more hard work.

On 23rd May, the suspense over the composition of the 17th Lok Sabha came to an end. The incumbent dispensation has come back with a larger majority and a wider acceptability. The results of the 17th general elections, according to me, have put many issues at rest. The message given by the public is unambiguous and has busted many a myth; the public would not desert a leader who is decisive and has the courage to take bold decisions (in the context of demonetisation and GST).

The Hon'ble Prime Minister has, as usual, sprung a surprise by picking up Mrs. Nirmala Sitharaman as the Finance Minister. She has become the second woman Finance Minister of the country, the first being, Mrs. Indira Gandhi. Mrs. Sitharaman is appreciated for her work in the Defence Ministry. Mrs. Sitharaman, has her plate full of challenges; the data put forward in the public domain recently indicates that the growth rate has slowed down and we are faced with an unprecedented level of joblessness. This has pushed the Reserve Bank of India to cut down the Repo Rate, to boost economic activity. The experts in the field feel that the efforts on the part of the regulator itself may not trigger growth in consumption to push the economic activity; the government may have to pitch in and facilitate economic activity. Ms. Nirmala Sitharaman's track record shows that she is an appropriate pick for the job to face these challenges. We all know that under her watch, the Balakot strike had been successfully carried out. Similar precision is required for handling the economic situation of the nation, especially when the financial sector is under severe stress due to mounting NPAs, crisis at ILFS, etc. On behalf of The Chamber of Tax Consultants, we wish the Hon'ble Finance Minister, all the best and assure support from an association which has a vibrant membership of advocates and Chartered Accountants.

Mr. Hinesh Doshi has successfully led The Chamber of Tax Consultants for a year and has taken it to greater heights. I congratulate him for this. I wish all the best to the incoming team. I thank all the contributors to this issue for sparing their valuable time.

K. GOPAL
Editor

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From the President

My dear Members

'Les mots de l'année prochaine attendent une autre voix. Et pour finir, c'est pour commencer!'

… In French means, ***Next year's words await another voice. And to make an end, is to make a beginning!***

It is always said - 'Time flies!' and I'm in the most relatable situation today to understand that. I would like to start from exactly where my friend Ajay Singh left of from, when he had concluded by saying – *'Surround yourself with people who have dreams, desire and ambition; they'll help you push for and realize your own!'* I would like to thank Ajay bhai, and The Chamber for passing over the baton to me with trust and awe and I have tried my best to serve The Chamber and its members wholeheartedly.

This will be my last communication to members. In my first communication in July, 2018, I had mentioned four Pillars of The Chamber namely: programmes, membership, visibility, team and vision. We have tried to focus and grow on all 4 pillars. Much sharper focus needs to be given to membership growth, and aggressive efforts are required using AI, Social media, digital analytics, etc. This year has been a journey filled with joy and a road leading The Chamber as an institution towards achieving even greater heights and touching newer horizons.

Showcasing and running through a quick recap, this year has been instrumental and special for The Chamber in varied and many ways. While this year witnessed many 'firsts', the continuing events and activities saw an increasing trend in every way.

…GROWTH IS THE ONLY CONSTANT

While many say, 'Change is the only constant!' I would take the liberty to amend the proverb a little and make it, ***'Growth is the only constant!'***, which to say it really is! And seeing a growing trend has become The Chamber's defining power and happens to be its strongest Unique Selling Proposition (USP).

This year proved to be a year filled with seminars and webinars covering a wide variety of topics increasing our professional knowledge base, student events ranging from sports, debate to moot court to essay writing competitions, members talent programme to technology awareness programmes to Self improvement series. This year also focused on growing the number of education hours along with increasing the number of programmes held and also new locations like Nagpur, Amravati etc.

While, the total number of education hours also saw an increase and ***crossed the thousand hours mark taking it to a total of 1,128 hours*** almost thrice compared to the previous years, total number of events held during the year also marked an increase. ***Out of a total number of 300 working days, the CTC has held events on 204 days,*** which happens to throw light on the fact that CTC held ***events and activities for nearing three-fourth of the total working days*** during the year.

The RRCs too have seen an increased participation over the years and have broken all previous records of registrations. ***This year, all past records of enrolments in all RRCs and International Study Tour are broken by a huge margin, t***he Direct tax RRC saw a total participation of 234 delegates, GST RRC saw a total participation of 221 delegates, while International tax RRC will see total enrolments of 300 + delegates. The 5th International Study tour to Central Europe saw highest ever enrolment of 91 delegates. This shows the

popularity of The Chamber and RRCs have become an annual feature for meeting of members for networking and bonding their relationship.

The iconic Dastur Essay Competition held by Chamber every year, to awaken the writers within students and allow their thoughts to flow freely, also saw an exorbitant rise in participation. This year, a total number of 462 registrations were recorded, nearly double compared to the last year.

The Chamber also held a variety of seminars and lecture meetings on the trending topics such as the Ind AS, NFRA rules, Advanced MLI and FEMA Course, the IBC Act, the New Benami Law and Prevention of Money Laundering Act, Study Course on Interpretation of Taxing Statutes and Valuation Course, apart from regular programmes on Income and Companies Act. We also conducted a lecture meeting on "Current Economic Scenario and Ease of Doing Business in India!" and Investor Awareness programmes for our members of Capital Market Study Circle.

Representations are our biggest forte and we continued submitting several representations, Writ Petitions, Memorandums, RTI etc. in the interest of tax payers, without fearing consequences. The Chamber filed ***writ petition*** and Hon'ble Bombay High Court passed Order on the petition filed by us on CBDT's proposal, where CIT-A would now be incentivised on passing 'quality' orders. As this would be detrimental to the interest of tax payers, the Hon'ble Bombay High Court has passed Orders for withdrawal of such Circular.

For outstation members and to promote digital information, The Chamber conducted several webinars in varied areas of interest. Self improvement lecture meetings on developmental aspects of life like – "Work, Play, Inspire, Repeat!", "Life is Beautiful!" and "Dynamic Memory". Upgrading members with new skills like blog writing, LinkedIn, ethical hacking, etc. To encourage the oratory skills among students, the CTC also organised an inter-college debate competition with 24 teams participating in the nail-biting standoff, three days Students Orientation Programme at Mulund & Vile Parle to train article students with basic training and also, the 3rd edition of Dr. Y. P. Trivedi National Moot Court Competition judged by two sitting Judges of Bombay High Court.

We also organized three industrial visits to the manufacturing units of Volkswagen car factory, Parag Milk Foods and CTRLs Data Center to get an insight as to how the operations at these iconic plants and centers are exactly carried out. Delhi Chapter and both Study Groups at Pune and Bengaluru are very active and serving local members.

As much as gaining knowledge is important for our profession, maintaining a work-life balance, getting some recreation is equally important. This year, the CTC has for the first time organized an Inter Firm Box Cricket Tournament, getting an overwhelming response with 34 teams (including 6 women teams), and Inter Firm Football Tournament with 24 teams (including 6 women teams), participating in the competition.

The Chamber organised outstation programmes and Conferences at Goa, Jamnagar, Kolhapur, Solapur, Nagpur, Kalyan, Amravati etc. with local professional organisations and associations for spreading knowledge.

THE FIRSTS

In Lao Tzu's words – *'A journey of a thousand miles begins with a single step!'*

And we tried taking some of those baby steps this year to turn it into a larger picture down the years, we tried sowing some new seeds this year, which would down the years turn into beautiful big trees yielding sweet fruits.

While, this year saw first time new initiatives, where a ***Technology clinic*** was set up, we also announced a ***Japanese language conversation course***, started ***two new Study Groups this year*** at Bengaluru and Hyderabad, held ***Conferences at new locations*** like Nagpur and Amravati-Jalgaon etc., ***Redesigned CTC News*** with new look completely to get Advertisement revenue, launched e-journal subscriptions for life members etc.

While, The Chamber set new records and surged towards growth, we shouldn't forget the people contributing to The Chamber, giving their valuable time to make all the events successful and its activities,

fruitful. I would like to extend my heartfelt gratitude to the office bearers, core committee members, chairpersons and all the members without which CTC couldn't have functioned the way it did, the entire year. ***"You don't build Institutions, you build people and then….. People build the Institution".*** I offer heartfelt thanks to the staff of CTC for being part of this wonderful family.

This year, we also tried to personify globalization by quoting every month's message and newsletter with a different language from different part of the world. As we understand, the world is now coming closer and the whole world is now in fact a global village.

To signify this, we tried covering twelve ancient and the most spoken languages in the world which have in some way, shaped and defined this beautiful planet. The languages we covered during this year were - Sanskrit, Latin, Chinese, Greek, Russian, Japanese, Hebrew, Korean, Turkish, Arabic, Spanish and French.

Though, in different languages but all countries, all languages, all sects have this one quote in common which says – ***"Learning never stops! Knowledge never ages!"***

We have recently witnessed absolute majority to the ruling party in recent elections 2019. India ranked 30th on WEF global manufacturing Index in 2017-18 and is expected to become the 5th largest manufacturing country in world by the end of 2020. India is likely to become the world's second-largest economy by 2030, next only to China and overtaking the US. To make India progress in every sphere, the next logical step to 'Make in India' would be 'Brands of India'. A new slogan to 'Jai Jawan, Jai Kisan' is 'Jai Vigyan!' and 'Jai Anusandhan' which means Science and Research. And it will be these reforms that will help India reach and climb the ladder of global ranks in varied areas. I see a very bright future for India and we all will witness this historic moment during our lifetime.

My dear members, the end is near! And as I write this last message to you, I realize it is time to bid an *adieu*. It's time to say a good bye with uncountable memories. But good byes are imminent and necessary, for without a good bye, there can be a no new beginning. And to start something new, we need to have an ending. In Paulo Coelho's words – *'If you're brave to say good bye, life will reward you will a new hello!'*

And as much as I would want to keep writing and conveying my thoughts in this last message to all my dear folks, knowing I wouldn't be able to do it any further, any more but following A. P. J. Abdul Kalam's words – *'Good byes should be short, really short!'* and I'd like to add, *'Impactful, pleasant and happy!'*

When people are financially invested, they want a return. When people are emotionally invested, they want to contribute. It is this emotional investment that has and always will hold us strong for the forthcoming year and many more years to come!

Special Story for this month on ***"Shares and Securities – Part II'*** will be useful for members. I thank Mr. Bhadresh Doshi, Mr. Vipul Choksi and Mr. Anish Thacker for preparing the design and structure of this special story, and also senior Authors who have spared their time and made timely contribution.

During this journey of one year, there would been several unintentional errors or mistakes. I entirely take blame and responsibility for them and hope you will pardon me.

With this, I would like to invite the next president Vipul Choksi and his team, placing confidence that he'll make The Chamber reach even newer horizons, and with some great positivity, hope, uncountable memories, love and one last food for thought – *'We cannot go back and make a brand new start but we can surely start from now and make a brand new ending!'* - I would like to say a thank you, and bid you all, a good riddance.

In twelve languages from around the world – I would like to express my gratitude for everything that Chamber has given me.

धन्यवादः gratias tibi 谢谢 ε υ χ α ρ ι σ τ ώ ありがとうございました תודה 고맙습니다
teşekkür ederim شكرا جزيلا благодарю вас gracias Je vous remercie

Pranam

Hinesh R. Doshi
President

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Taxation of Derivatives

Introduction

Based on the L.C. Gupta Committee recommendations, the Indian government allowed trading in derivatives on the stock exchanges from June 2000.

'Derivative' is an instrument whose value depends on its underlying cash or physical asset. Hence, it means that the value is derived from the value of the underlying assets like foreign exchange, currency, securities and commodities. It also includes market indices such as the BSE Sensex or benchmark interest rates, etc. The result of a derivative transaction is transfer or exchange of specified cash flows at defined future points in time.

Typically, derivatives are used to hedge against price, currency and interest rate risk. Derivatives can also be used for speculative functions.

There are four commonly traded derivative instruments:

1. **Forward contract:** It is an agreement to buy or sell an asset at a certain future time for certain price. These are traded over the counter (OTC).

   Example: P agrees to purchase from Q 100 shares of 'R Ltd' on a fixed future date for a pre-determined price of say ₹ 10. Here, on the fixed future date, P will pay ₹ 10 to Q and Q will deliver the shares of R Ltd to P.

2. **Future contract:** A financial future contract is an agreement between two parties to buy or sell standard quantity of specific asset at a future date at a price agreed between the parties through an organized future exchange.

   Example: X enters into a future contract to purchase shares of Z Ltd at ₹ 10 on 31st December. If for instance, on 31st December, the price of Z Ltd is ₹ 9, then X will pay ₹ 1 per share. If the price of Z Ltd is ₹ 12 then X will get ₹ 2 per share.

3. **Option**: The holder of option has the right, but not the obligation, to buy or sell the underlying asset at the fixed rate (i.e., strike price) at a future date. Correspondingly, the writer of the option has the obligation to buy or sell the underlying asset on the agreed date at the strike price basis the option exercised by the holder of the option.

   Example: In above example, if the price of Z Ltd on exercise date is ₹ 12 then X will

exercise the option as he stands to benefit from doing so. However, if the price falls to ₹ 9 then he will not exercise the option, thus restricting his loss to the amount of the premium paid by him.

4. **Swap**: A swap means a financial transaction in which two counterparties agree to exchange the streams of payment or cash flows, over a time.

   Example: P has borrowed from Q at MIBOR + 4%. P now desires a fixed rate of interest at about 12%. R on the other hand is willing to borrow at MIBOR + 4% and lend at 12%. In a swap transaction between P and R, only the interest payments are exchanged on net basis whereas the actual principal amounts are never exchanged.

   Having discussed the concept of derivative securities, let us now understand how these derivative securities are taxed under the Income-tax Act, 1961 (Act).

Taxability

General provisions

Indian residents are subject to tax on their worldwide income while non-residents, on the other hand, are taxed only on income received by them in India, or income that accrues or arises to them in India. Further, under certain conditions, income can be "deemed to accrue or arise in India" and thereby be subject to tax in India.

Derivatives taxation

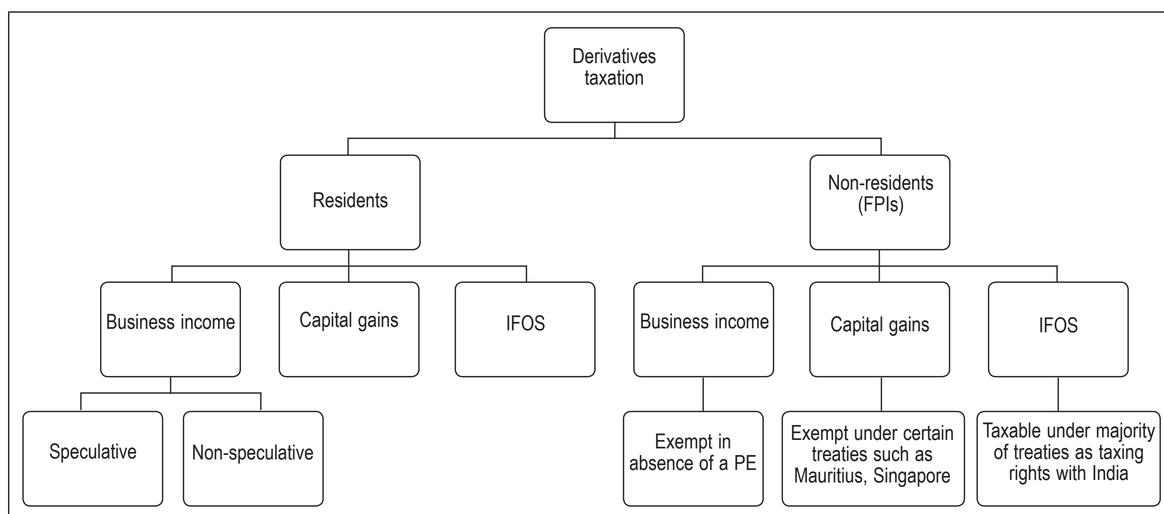
There are no specific rules governing the taxation of derivatives contracts.

However, the following issues are relevant in taxation of a derivatives transactions:

1. Characterisation of income i.e., business income or capital gains or income from other sources.

2. Determination of income i.e., timing and cash flow.

A diagrammatic representation of the taxability of derivatives has been provided below:



Characterisation of income

Income arising from derivatives may be treated either as 'capital gains' or as 'business income' or 'income from other sources' for income-tax purposes, depending upon whether such securities are held as capital asset or stock-in-trade.

Readers may refer to the following CBDT communications providing guidance on the characterisation of income:

- Instruction No. 1827, dated 31st August, 1989.
- Office memorandum dated 13th December, 2005.
- Circular No. 4/2007, dated 15th June, 2007.
- Circular No. 6/2016, dated 29th February, 2016.
- Letter F. No. 225/12/2016/ITA.II, dated 2nd May, 2016.

The aforesaid communications have also been dealt with in The Chamber's Journal of April 2019 on Shares and Securities – Part-I in article 'Capital Gains vs. Business Income' by CA Kiran Nisar.

We have in the ensuing paragraphs discussed the various aspects on the characterisation of income.

Business income

Where income from derivative transactions is classified as business income, it can be further classified as:

(a) income from speculative transaction; or

(b) income from non-speculative transaction.

As per the provisions of section 43(5) of the Act, a speculative transaction means a transaction in which a contract for the purchase or sale of any commodity including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips.

However, the below transactions though settled otherwise than by actual delivery are not regarded as speculative transactions:

- Trading in eligible derivatives including commodity derivatives;
- Hedging contract in respect of stocks and shares;
- Trading in eligible forward contract.

The meaning of speculative transactions along with exceptions has been explained in The Chamber's Journal of April 2019 on Shares and Securities – Part I in Article 'Speculative Transactions' by CA Kalpesh Katira and CA Prathmesh Pokharankar.

The distinction of speculation transaction is important given the specific provision under section 73 of the Act i.e., speculation loss can only be set-off against speculation gains and are allowed to be carried forward only for a period of 4 years.

Tax rates

We have briefly discussed the tax rates for business income as under:

Person	*Tax rate*
Resident individuals	Applicable slab rates
Resident companies	25%/30%
Non-resident companies	40%
Treaty eligible person	Typically exempt in absence of a permanent establishment in India

Note: *The rates mentioned in this article are excluding applicable surcharge and cess.*

We shall now discuss the compliances to be undertaken by an assessee (including by a foreign company) where an assessee earns business income.

Maintenance of books of account

As per the provisions of section 44AA of the Act, where business income exceeds ₹ 1.2 lakhs, the assessee is required to maintain books of account.

Tax audit

As per the provisions of section 44AB of the Act, where the turnover exceeds ₹ 1 crore, the assessee is liable to get his books of accounts audited.

Presumptive taxation

As per the provisions of section 44AD of the Act, if the turnover is less than or equal to ₹ 2 crore then the income from these transactions can be taxed under the presumptive taxation scheme. In such cases, the assessee is exempted from maintenance of books of account and having the same audited.

In the context of income from derivatives, it becomes relevant to understand how the turnover shall be computed for the purposes of aforesaid sections which has been discussed below.

Meaning of turnover

As per the guidance note on tax audit issued by The Institute of Chartered Accountants of India (ICAI), the turnover in case of derivative transactions is determined as follows:

- **Non-delivery based**: Total of absolute values of profits and losses.
- **Delivery based**: Total of sales value.

Capital gains

Where income from derivatives transactions is classified as capital gains, it may be further classified as short-term or long term in nature depending on the period of holding as follows [section 2(42A) of the Act]:

Derivatives	*Short-term*	*Long-term*
Listed	Up to 12 months	More than 12 months
Unlisted	Up to 36 months	More than 36 months

Typically, the derivatives are for a period up to 12 months and are short-term in nature.

The distinction of short-term and long-term is important given the specific provision under section 70 and section 74 of the Act i.e., long-term capital loss can only be set-off against long-term capital gains whereas short-term capital loss can be set-off against both short-term and long-term capital gains. Further, the said losses are allowed to be carried forward for a period of 8 years.

Specific provision applicable for non-residents being Foreign Portfolio Investors (FPIs)

As per the provisions of section 2(14) of the Act, every security is deemed to be a 'capital asset' for FPIs and typically, gains/losses from trading in derivatives is subject to tax under the head 'Capital Gains'. However, in case of swaps, there is a possibility of same being classified as 'Business Income' or 'Income from Other Sources' (discussed in detail in subsequent paragraphs).

Tax rates

We have briefly discussed the tax rates for short-term capital gains as under:

Person	*Tax rate*
Resident individuals	Applicable slab rates
Resident companies	25%/30%
Non-residents companies	40%
FPIs	30%
Treaty eligible person	Exempt in certain treaties discussed below

We have illustrated below certain treaties which have a favourable treatment for taxation of derivatives i.e., gains from derivatives are exempt:

Sr. No.	*Country*
1	Mauritius
2	Singapore
3	Netherlands
4	Luxembourg
5	Colombia
6	Korea
7	Croatia
8	Cyprus
9	Bhutan

Having discussed the head of income under which gains from derivatives shall be taxed, a question arises as to when such income should be offered to tax and how such income should be computed.

Timing of taxation and determination of income

Timing of taxation

As per the provisions of section 145 of the Act, with respect to business income or income from other sources, an assessee has an option to follow mercantile or cash basis of accounting. Accordingly, income may be offered to tax by an assessee depending on the method of accounting adopted.

With respect to capital gains, an assessee may pay tax at the time of transfer of a capital asset.

Having understood when to offer the income to tax, let us now understand how to compute the income.

Business income

Typically, the business income is calculated as the difference between sales price and purchase price. For options, premium paid/received should also be taken into consideration.

However, for an assessee following mercantile system of accounting, a question arises as to whether unrealised marked to market gains/losses are to be considered.

In this regard, as per the provisions of Income Computation and Disclosure Standard (ICDS)-I, unrealised marked-to-market losses should not be recognised. Further, unrealised marked-to-market gains should also not be offered to tax.

Scheduled Banks, on the other hand, are governed by the provisions of Part-B of ICDS VIII. As per these provisions, securities including derivatives shall be recognised and measured in accordance with the Reserve Bank of India guidelines.

The provisions of ICDS have been explained in detail in The Chamber's Journal of April 2019 on Shares and Securities – Part I in article 'Impact of ICDS' by Adv. Dharan Gandhi.

Capital Gains

We shall now discuss the computation of capital gains for futures and options as under:

(a) Futures

For the purpose of computation of capital gain/loss on futures, only settled positions are considered. The short-term capital gains/loss on futures is calculated as the difference between sales price and purchase price.

We have discussed below the capital gains for futures in two scenarios:

Scenario 1: *Futures contract squared-off during the same financial year*

- **1st March, 2019:** Purchase of 100 quantity of a specified future contract
- **12th March, 2019:** Sale of 100 quantity of a specified future contract

The short-term capital gains or loss in the aforesaid scenario would be included in the total income for the financial year ended 31st March,

2019 i.e., the year in which the futures contract has been squared-off.

Scenario 2: *Futures contract squared-off in the next financial year*

- **15th March, 2019**: Purchase of 100 quantity of a specified future contract
- **21st April, 2019**: Sale of 100 quantity of a specified future contract

The short-term capital gains or loss in the aforesaid scenario would be included in the total income for the financial year ended 31st March, 2020 i.e., the year in which the futures contract has been squared-off.

The above approach would be similar where a futures contract is first sold, pursuant to which an 'unwind' transaction (i.e., buy transaction) is executed and a similar first-in-first-out (FIFO) methodology will be applied to match the initial sale and subsequent buy for the purpose of computing the gains/loss in such a scenario.

(b) Options

The premium received/paid and settlement of options on account of exercise or assign, may be considered as two separate events for the purpose of recognizing capital gains/losses.

Accordingly, the gains/loss arising on an option contract is computed as under and included in the total income in the relevant financial year at the point of each of the following events occurring:

Creation of the option contract

- **Sale of options (Options writer)**: The total premium received is treated as short-term capital gains on the date of the writing of the option (and included in the total income of the relevant financial year).
- **Purchase of options (Options buyer):** The total premium paid is treated as short-term capital loss on the date of the purchase of the option (and set-off against any other taxable capital gains of the relevant financial year).

Exercise/Assignment/Lapse of option contract

- **Where the options is exercised (in the money)**: The entire settlement amount (i.e., Market price *minus* Strike price*Qty) is considered as short-term capital gains on the date of the exercise of the option (and included in the total income of the relevant financial year when the option is exercised).
- **Where the option is assigned**: The net settlement amount (i.e., Strike price *minus* Market price*Qty) is considered as short-term capital loss on the date of the assignment of the option (and set-off against any other taxable capital gains of the relevant financial year in which the option is assigned).
- **Where the option lapses:** Not a taxable event and accordingly, no capital gains tax impact.

Alternatively, there exists another view that similar to futures transaction, capital gains event triggers only on the square-off or expiry of the options contract.

Having understood the determination of income and timing of taxation of derivatives, let us now understand the nuances around the taxability of certain types of derivatives.

Taxability of certain derivatives

(a) Taxability of swaps

While cancellation of swaps should qualify as 'business income' or 'capital gains' basis the discussions above, the characterisation of the amount of swap payments would need further evaluation.

As per section 2(28A) of the Act, interest income should be in respect of moneys borrowed or debt incurred.

In a swap transaction, there is no money borrowed or debt incurred. The principal of a swap deal is the notional amount and the adjustment takes place between the bank and the counter-party in respect of the amounts payable by them. Only the net amount changes hands.

Additionally, given the nature of swap transaction, there exists an ambiguity whether the same results in a transfer as defined under section 2(47) of the Act. In absence of any sale, exchange, relinquishment, extinguishment of a capital asset, the income cannot be characterised as capital gains.

Therefore, such amounts may qualify as trading income taxable as 'business income' or taxable under the head 'income from other sources'.

Where the income has been characterised as 'business income' compliance provisions discussed above would be triggered, which is a point of concern especially for the non-residents investors. Arguably, where the non-resident investors are from a treaty favourable jurisdiction and business income is claimed as exempt, then relying on judicial precedents there may be a possibility to argue that the machinery provisions of maintenance of books of account and having the same audited may not apply.

(b) Physical settlement of derivatives

The SEBI on 11th April, 2018 issued a Circular No. SEBI/HO/MRD/DP/CIR/P/2018/67 where derivative contracts (Futures and Options) in certain scrips were permitted to be settled by the physical delivery.

In this context, there is no clarity on whether there ought to be single tax event (at the stage of physical delivery of shares) or two tax events (first on expiry of derivatives contract and second at the stage of physical delivery of shares).

For the said purpose, it is relevant to understand the fund flow mechanics of physical settlement which has been detailed below:

- In case of a futures contract, on expiry, the clearing member debits the client's cash account by the settlement price (for cost of acquiring underlying shares) and credits/ debit MTM gain/loss – thereby implying two tax events of settlement of futures contract and physical delivery of shares.
- In case of an options contract, on expiry, the clearing member does not credit/debit the MTM gain/loss – thereby implying single tax event of physical delivery of shares.

However, taxability of physical derivatives contracts is grey and at a nascent stage. Accordingly, a comprehensive clarification by CBDT taking care of the taxability aspects would be welcoming.

However, the CBDT clarified that the rates of securities transaction tax (STT) as applicable to delivery-based equity transactions (being 0.1 per cent of the settlement price on purchase/ sale) should also be applicable to a derivatives contract which is settled by way of physical delivery of the underlying shares, thus indicating that the settlement of derivatives and receipt of shares pursuant to physical settlement should be viewed as two separate events.

Conclusion

Derivatives as an instrument is evolving in Indian markets. We are regularly seeing complex derivatives products being introduced in the Indian markets and believe that the tax law around the taxation of derivatives will evolve over a period of time. While in the course of the article above, we have tried to simplify the India tax regime applicable on various income streams from derivatives as applicable to different types of assessees, a tax practitioner may at times be required to apply the general principles of taxation and jurisprudence for taxation of derivatives products.

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CA Manoj Khetan

Anti-avoidance provisions on Securities

This article analyses the anti-avoidance provisions on securities contained in section 94 of the Income-tax Act, 1961 (the Act). The analysis is divided into 3 parts as under:

1. Sections 94(1) to 94(6) popularly known as "Bond Washing"
2. Section 94(7) popularly known as "Dividend Stripping"
3. Section 94(8) popularly known as "Bonus Stripping"

Bond Washing

Bond Washing – how it works?

In bond washing, the assessee owns debt securities. On the eve of the due date for payment of interest, he transfers his securities to a third person who receives the interest. After the receipt by the transferee of the interest, the assessee buys back the securities. The result is that the assessee though continuing to own the securities, avoids payment of tax on the interest.

Another type of bond washing happens where a person owning a security beneficially sells or disposes of the security or the income thereof in such a manner that he receives no interest in respect thereof for that year, or he receives an income which is less than what it would have been, had the interest been treated as accruing from day-to-day and apportioned accordingly to the transferor.

The difference between the former method and later method of bond washing is: in the former, there is a transaction of sale with a buy back. In the later, there is no buy back. There is simply a disposition of the security, shifting the right to receive the income to another person.

In both these methods, the assessee whose income falls under the highest tax slab finds a person who is either not liable to tax or liable to tax under the lowest tax slab to undertake the transactions of this nature. Also, the assessee sells the security at a price much lower than cum-interest price so that he earns no income or earns lesser income.

Enactment of sections 94(1) to 94(6) to curb avoidance of tax through bond washing

To curb avoidance of tax through former method as explained above, section 94(1) was enacted, as per which the interest is deemed to be the income of the transferor despite the transfer by him and is made chargeable in his hands. Conditions to be satisfied for trigger of section 94(1) are as follows:

a) The transferor should have sold the security in the first instance and bought back later. No time period prescribed within which the transferor should sell or buy back to trigger section 94(1).

b) In the interval, the dividend or interest should have been received or receivable by the transferee.

These deeming provisions are applicable irrespective of whether the interest would or would not have been chargeable to tax otherwise than under this section.

Securities for the purposes of section 94 has been defined in an inclusive manner to include stocks and shares.

Application of section 94(1) to similar securities

The Explanation to section 94(1) provides that the references to buying back or reacquiring the securities shall be deemed to include similar securities which means these provisions will apply not merely to transactions in identical securities but also to transactions in similar securities such that where similar securities are bought, the assessee shall be under no greater tax liability than he would have been if original securities had been bought back. The Explanation (c) after 94(6) contains the definition of similar securities.

Treatment in the hands of the transferees engaged in the business of dealing in securities for cases covered in section 94(1) to avoid double taxation

Section 94(4) provides that where the transferee under section 94(1) is a person engaged in the business of dealing in securities wholly or partly and the income from a transaction of sale and buy back of securities with such a transferee has been made liable to tax in the hands of the transferor under section 94(1), then such income will not be taxed again in the hands of the transferee. This is a logical result of section 94(1), and it has been statutorily enacted in section 94(4). In fact, section 94(4) goes one step ahead and exempts both in the hands of the transferee i.e., such income and the profit if any arising on sale of security to the transferor.

Dealing in securities resulting in non-receipt or diminution of income

Section 94 (2) is enacted to curb avoidance of tax through later method discussed above. Conditions to be satisfied to trigger section 94(2):

a) A person holds a beneficial interest in securities any time during the previous year.

b) He undertakes a transaction relating to such securities or the income arising therefrom.

c) Such that in respect of such securities within that year, either no income is received by him or the income received by him is less than what would have been if the income from such securities had accrued from day-to-day and been apportioned accordingly,

If the above conditions are satisfied, the income from such securities for such year shall be deemed to be the income of such person. Consequently, such income should not be taxable in the hands of any other person with whom the first mentioned person undertakes a transaction covered by section 94(2) though such exemption is not statutorily enacted on the lines of section 94(4).

Exemption from application of bond washing provisions

The provisions of sections 94(1) and 94(2) do not apply if the owner or the person who has had a beneficial interest in the securities proves to the satisfaction of the Assessing Officer (a) that there has been no avoidance of income-tax, or (b) that the avoidance was exceptional and not

systematic, and that in his case in any of the three preceding years, there was no avoidance of income-tax by a transaction of the nature referred to in these sections.

Procedure

These provisions are brought into operation by the Assessing Officer issuing a notice is writing to the taxpayer requiring him to furnish all such particulars as he considers necessary in respect of the securities which the assessee owned during the relevant year or in which he held any beneficial interest at any time during the said year to ensure that due taxes in respect of dividend or interest on such securities has been paid by him. The Assessing Officer should give time of at least 28 days for compliance with the notice.

Note: While bond washing may have been used to avoid tax on interest income on debt securities, the scope of anti-avoidance provisions contained in section 94(1) and 94(2) cover both interest income on debt securities and dividend income on shares. So, if an assessee tries to avoid tax on dividend income on shares in a manner given in section 94(1) and 94(2), then these anti-avoidance provisions will equally apply to such case.

Dividend Stripping – how it works?

Dividend stripping is an attempt to reduce the tax liability, by a person who purchases *securities* and *units* just before the record date and receives dividend/income exempt under the Act, and sells after the record date at a price lower than the price at which, such securities/units were purchased and incurs a loss which can be set off and carried forward. This practice of claiming double benefit is popularly known as "Dividend Stripping". To curb such practice, section 94(7) was enacted by Finance Act 2001 with effect from assessment year 2002-03.

Conditions to be satisfied to attract provisions of Dividend Stripping

Conditions	***Securities***	***Units***
Buying or acquiring - (94(7)(a))	Within a period of **3 months** prior to the record date	Within a period of **3 months** prior to the record date
Selling or transferring - (94(7)(b))	Within a period of **3 months** after the record date	Within a period of **9 months** after the record date
Dividend or income during intervening period - (94(7)(c))	Exempt	Exempt

Notes:

1. Provisions contain the definitions of "unit" and "record date" as under:

   (a) The definition of "unit" makes reference to clause (b) of the Explanation to section 115AB for its meaning. The said clause defines "unit" as follows: *"unit"* means *unit of mutual fund specified under clause (23D) of section 10 or of the Unit Trust of India.*

   (b) "record date" means such date as may be fixed by—

      (i) a company for the purposes of entitlement of the holder of the securities to receive dividend; or

      (ii) a Mutual Fund or the Administrator of the specified undertaking or the specified company as referred to in the Explanation to clause (35) of

section 10, for the purposes of entitlement of the holder of the units to receive income, or additional unit without any consideration, as the case may be;

2. Provisions originally enacted by Finance Act 2001 required a person to hold units for at least 90 days after the record date however it did not provide the desired effect and accordingly, to provide further deterrence to tax-avoidance, longer holding period of 9 months after the record date was replaced by Finance Act 2004 with effect from assessment year 2005-06.

3. The above conditions need to be satisfied cumulatively to attract the provisions of section 94(7).

4. Provisions of section 94(7) will not apply:

a) If the securities are bought before 3 months prior to the record date and sold after 3 months from the record date.

b) If units are bought before 3 months prior to the record date and sold after 9 months from the record date.

Consequence if the above conditions are satisfied
If the above conditions are satisfied, then

1. Loss, if any, arising on sale of such securities or units, to the extent such loss does not exceed the amount of dividend or income received on such securities or unit, needs to be ignored.

2. Loss in excess of dividend or income received on such securities will be allowed to be set off and carried forward.

Section 94(7) does not make distinction between the holding of securities/units as capital assets and as stock-in-trade and hence, the same should be applicable to both an investor and trader of securities/units.

Practical illustrations on Dividend Stripping
Given below are practical illustrations to help understand these provisions better:

Particulars	*Illustration 1*	*Illustration 2*	*Illustration 3*	*Illustration 4*
	Securities (Shares)	*Securities (Shares)*	*Units*	*Units*
Quantity	1000	1,000	1000	1000
Purchase date	31st March 2018	30th April 2018	31st May 2018	30th June 2018
Price per share/ unit (₹)	120	120	120	120
Total purchase price (₹)	120,000	120,000	120,000	120,000
Record date	28th June 2018	28th August 2018	28th August 2018	28th September 2018

Particulars	***Illustration 1***	***Illustration 2***	***Illustration 3***	***Illustration 4***
	Securities (Shares)	*Securities (Shares)*	*Units*	*Units*
Dividend per share/unit (₹)	20	20	20	20
Total dividend (₹)	20,000	20,000	20,000	20,000
Sale date	25th September 2018	24th November 2018	25th May 2019	25th July 2019
Price per share/ unit (₹)	90	90	100	110
Total sale price	90,000	90,000	100,000	110,000
Gain/(Loss) on sale = sale price – purchase price (₹)	(30,000)	(30,000)	(20,000)	(10,000)
Sec 94(7) attracted?	Yes[1]	No[2]	Yes[3]	No[4]
If yes, loss allowed?	Yes	NA	No	NA
If yes, amount (₹)	(10,000)	(30,000)	Nil	(10,000)

Applicability of Dividend Stripping provisions in cases where the dividend received is taxable in the hands of the person under section 115BBDA of the Act

Finance Act 2016 enacted section 115BBDA with effect from assessment year 2017-18 to provide that where the total income of an individual, HUF or a firm resident in India includes dividend income exceeding ten lakh rupees from a domestic company or companies in aggregate, then such dividends in excess of ten lakh rupees shall be taxable at the rate of 10% (plus surcharge and cess) on gross basis.

So, in a case where an individual, HUF or a firm resident in India, undertakes a Dividend Stripping transaction in shares and the dividend income received during the intervening period of such transaction is taxable in his hands under section 115BBDA, then in such a case, condition as per section 94(7)(c) will not be satisfied to trigger section 94(7) and accordingly, the entire loss arising from sale of such shares may be allowed to be set off or carried forward. This position may be litigated by the tax authorities given that dividend is taxable at a concessional rate of 10% whereas short term capital loss or business loss can help save tax at a rate higher than 10%.

It may be pertinent to note that dividend received from the domestic company alone is covered by section 115BBDA and dividend received on units is not covered by the said section.

1. Conditions as per section 94(7) (a) to 94(7)(c) are satisfied
2. Condition as per section 94(7)(a) is not satisfied
3. Conditions as per section 94(7) (a) to 94(7)(c) are satisfied
4. Condition as per section 94(7)(c) is not satisfied

Some Key Jurisprudence on Dividend Striping provisions

1. In case of *Walfort Share and Stock Brokers P. Ltd. (192 Taxman 211 (SC))*, the Supreme Court, while dismissing the department appeal, *inter alia* held that:

    a) The argument of the department that the transaction was entered into in a pre-meditated manner and that the loss is not genuine is not acceptable. Even assuming that the transaction was pre-planned, there is nothing to impeach the genuineness of the transaction. With regard to *McDowell & Co 154 ITR 148 (SC),* in the later decision in *Azadi Bachao Andolan 263 ITR 706(SC)* it has been held that a citizen is free to carry on its business within the four corners of the law. Mere tax planning, without any motive to evade taxes through colourable devices is not frowned upon even in McDowell & Co. Accordingly, the losses pertaining to exempted income cannot be disallowed prior to insertion of section 94(7).

    b) The argument of the department that the loss constitutes "expenditure incurred" for earning tax-free income and was liable to be disallowed u/s. 14A is not acceptable. The difference arose as a result of the dividend pay-out. The said "pay-out" is not "expenditure" to fall within section 14A. For attracting section 14A, there has to be a proximate cause for disallowance, which is its relationship with the tax-exempt income, which is absent in the present case.

2. In case o*f CIT vs. Mr Sarosh Nowrojee Burjorjee (TS-802-HC-2014 (KAR))*, the limited issue before the High Court was whether the words "such date" used in clause (b) of section 94(7) of the Act refers to "record date" (as per tax authority's view) or "date of purchase of shares" (as per Tax Payer's view). The High Court held that "such date" referred in section 94(7)(b) refers to "date of purchase of shares". In the case before High Court, the sale was admittedly beyond 3 months from the date of purchase and hence, provisions of section 94(7) were not attracted. Consequently, the benefit of deduction of loss was allowed.

3. In case of *ITO vs. Shambhu Mercantile Ltd. (304 ITR (AT) 36)*, Delhi bench of the Tribunal held that for provisions of section 94(7) of the Act to be triggered, conditions prescribed in clauses (a) to (c) to section 94(7) need to be satisfied cumulatively. This decision has been subsequently upheld by Delhi High Court (325 ITR 535).

4. In case of *Smt. Rohini Nilekani vs. ACIT (35 Taxman 536),* Bangalore Bench of the Tribunal held that when there are two record dates between date of purchase and sale of units, first record date should alone be considered for applicability of provisions of section 94(7).

5. In case of *Carissa Investment (P) Ltd. vs. ITO (83 Taxman 172)*, the assessee was having huge opening balance of shares (approx. 1.40 crores) of one of the companies coming from earlier years and during the year, the assessee purchased 5,65,864 shares. As against such huge holding of shares, only 16,50,414 of these shares were sold. On these facts, Delhi Bench of the Tribunal held that *prima facie* it cannot be reckoned that the loss on sale is only on account of the shares which were held for less than period of three months. Given this aspect was not

examined by the lower authorities, the Tribunal restored the matter back to the file of the Assessing Officer.

Bonus Stripping

After enactment of dividend stripping provisions, it was realised that avoidance in the form of deferral of tax is possible in the context of issue of bonus units, since receipt of bonus units is exempt and price of units ordinarily fall after such bonus issue. It is possible for the assessee to sell the original units at a loss, while retaining bonus units with full cost being allowed on sale of original units in view of section 55(2)(aa)(iiia) inserted by Finance Act 1995 with effect from assessment year 1996-97 treating bonus units and original units as distinct categories of assets.

To prevent such practice of bonus stripping in respect of units, section 94(8) was enacted by Finance Act 2004 with effect from assessment year 2005-06 to provide that the loss on sale of original units where bonus units have been issued will be ignored and the amount of such loss shall be considered as the cost of acquisition of the bonus units subject to the prescribed conditions.

Conditions to be satisfied to attract provisions of Bonus Stripping

Conditions	*Units*
Bought or acquired (Original units) – 94(8)(a)	Within a period of **3 months** prior to the record date
Allotment of additional units (Bonus units) – 94(8)(b)	Without any payment on such record date
Sold or transferred (Original units) – 94(8)(c)	Within **9 months** after the record date
Holds at least one additional bonus unit – 94(8)(c)	On the date of such sale or transfer of original units

Notes:

1. The above conditions need to be satisfied cumulatively to attract the provisions of section 94(8) of the Act.
2. Provisions of section 94(8) are not applicable if units are bought before 3 months prior to the record date and sold after 9 months from the record date.
3. Provisions of section 94(8) are not applicable if all the bonus units are transferred before the original units are transferred or on the same day when original units are transferred.
4. Provisions of section 94(8) are applicable only to units and not to shares.

Consequence if conditions related to Bonus Stripping are satisfied

If the above conditions are satisfied, then, the loss, if any, arising on sale of all or any of original units needs to be ignored and the amount of loss so ignored will be deemed to be the cost of purchase of such bonus units as are held by him on the date of sale or transfer of original units.

Section 94(8) does not make distinction between the holding of units as capital assets and as stock-in-trade and hence, the same should be applicable to both an investor and trader of units. If the person holds such units as capital assets, benefit of indexation can be claimed on such cost of acquisition subject to the indexation provisions contained in section 48 of the Act.

Practical illustrations on Bonus Stripping

Illustration-1

ABC Mutual Fund declares 1:1 bonus units on its units on 30th April, 2018. The record date for bonus units issue is fixed to be 31st of May, 2018. Mr. X purchases 10,000 units (original units) of ABC Mutual Fund on 15th May, 2018 at a rate of ₹ 50 per unit. Mr. X sells 10,000

original units on 15th December, 2018 at a rate of ₹ 40 per unit. Mr. A holds the units as capital assets.

Sr. No.	Particulars	Amount in ₹
1	Sales value (10000 x 40)	4,00,000
2	Cost of acquisition (10000 x 50)	5,00,000
3	**Short term capital loss (1-2)**	**(1,00,000)**
4	No. of bonus units	10,000

Consequence

Short-term capital loss amounting to ₹ 1,00,000/- shall not be allowed to set off or carry forward. Instead, the same shall be considered as cost of acquisition of 10,000 bonus units.

Illustration – 2

If in the above illustration, Mr. X sells 10,000 original units and 7,000 bonus units on 15th December, 2018 at a rate of ₹ 40 per unit then:

Sr. No.	Particulars	Amount in ₹	
		Original units (10,000)	***Bonus units (7,000)***
1	Sales value	4,00,000	2,80,000
2	Cost of acquisition	5,00,000	0
3	**Short term capital (loss)/ gain (1-2)**	**(1,00,000)**	**2,80,000**

Consequence

Short-term capital loss amounting to ₹ 1,00,000/- shall not be allowed to set off or carry forward. Instead, the same shall be considered as cost of acquisition of 3,000 bonus units that Mr X continues to hold when the original units are transferred. Short-term capital gain amounting to ₹ 2,80,000 on sale of bonus units shall be taxable.

Illustration – 3

If in the illustration 1, Mr. X sells 10,000 original units and 10,000 bonus units on 15th December 2018 at a rate of ₹ 40 per unit then:

Sr. No.	Particulars	Amount in ₹	
		Original units (10,000)	*Bonus units (10,000)*
1	Sales value	4,00,000	4,00,000
2	Cost of acquisition	5,00,000	NIL
3	**Short term capital (loss)/ gain (1-2)**	**(1,00,000)**	**4,00,000**

Consequence

In this case, the provisions of section 94(8) are not applicable since as on the date of sale of original units, Mr X does not hold any bonus unit. Hence, the short-term capital loss amounting to ₹ 1,00,000 on sale of original units shall be allowed to be set off and carried forward. The short-term capital gains amounting to ₹ 4,00,000 on sale of bonus units shall be taxable.

Bonus Stripping in shares and General Anti Avoidance Rule (GAAR)

As mentioned above, bonus stripping in units alone is covered by section 94(8) and bonus stripping in shares is not covered by the said section.

After introduction of GAAR effective from assessment year 2018-19 onwards, it may be debatable whether bonus stripping in shares will now be covered by the GAAR provisions.

One view may be that if legislature in its wisdom decided to apply dividend stripping provisions to both shares and units but

restricted application of bonus stripping provisions only to units, then there may be an intention to allow the loss arising from bonus stripping in shares.

Other view may be that the GAAR provisions are wide in scope and apply to an impermissible avoidance arrangement (IAA). IAA means an arrangement, the main purpose of which is to obtain a tax benefit which includes deferral of tax, and meets other specified criteria such as abuse of the provisions of this Act, lacks commercial substance etc. An arrangement is presumed, unless it is proved to the contrary by the assessee, to have been entered into, or carried out, for the main purpose of obtaining a tax benefit, if the main purpose of a step in, or a part of, the arrangement is to obtain a tax benefit, notwithstanding the fact that the main purpose of the whole arrangement is not to obtain a tax benefit.

The threshold limit for GAAR provisions to get triggered is aggregate tax benefit of ₹ 3 crores arising from an arrangement in the relevant assessment year.

General perception of dividend stripping and bonus stripping transactions is that they are undertaken with the main purpose of obtaining a tax benefit. The GAAR provisions do not contain any objective criteria to prove to the contrary. Absent such criteria, the assessee may find it difficult to prove to the contrary. In such a case, subject to the threshold limit, the Tax Authorities may take a view that bonus stripping in shares is covered by the GAAR provisions which may give rise to tax litigation.

Some Key Jurisprudence on Bonus Striping provisions

1. In case of *DCIT vs. Ghanshyam Dass Seth (26 SOT 166)*, Delhi Bench of the Tribunal held that the provisions of section 94(8) have to be applied with effect from 1-4-2005 i.e., operative from the assessment year 2005-06. Since the assessment year under consideration was 2003-04, the same shall not be applicable in this appeal. The instances defined in section 94 (7) are distinct from instances defined in section 94(8) and therefore, the transaction in question of the assessee would fall in category of transaction prescribed in section 94(8).

2. In case of *DCIT vs. B. G. Mahesh (43 Taxman 158)*, Bangalore Bench of the Tribunal held that since section 94(8) covered only 'units' and not 'securities', assessee's claim for set off of loss on sale of shares after receipt of bonus shares cannot be disallowed.

Conclusion

In summary, provisions of section 94(1) and 94(2) may have limited relevance in the current context given that pricing of debt securities at the time of sale generally factors in the interest accrued till the date of sale which in commercial parlance is known as cum-interest price and dividend is exempt. Dividend and bonus stripping provisions though enacted from assessment years 2002-03 and 2005-06 respectively, jurisprudence around these provisions is still evolving. Karnataka High Court's decision on the interpretation of words "such date" referred to in section 94(7)(b) is one such example. Clarification from the Board on the applicability of the dividend stripping provisions to cases covered by section 115BBDA and of the GAAR provisions to bonus stripping in shares will provide certainty and avoid unnecessary tax litigation.

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Angel Tax – A stumbling block in the start-up growth story

Introduction

Angel Tax has become one of the most debated issues today in the Indian business context. Since the time these provisions were introduced in 2012, there have been constant representations from the industry that they be abolished. However, the provisions continue to apply currently – albeit with certain relaxations – and since the controversy around Angel Tax is not likely to go away any time soon, we have attempted to analyse the rationale for introduction of the tax, the chasm between how it was conceived *vis-a-vis* its actual implementation, and how the opinions and actions of the various stakeholders, i.e, the Government, courts, start-ups and investors, are shaping the tax landscape.

The Concept

Angel Tax or Section 56(2)(viib) of the Income-tax Act, 1961 (the Act) aims to tax the consideration received by closely held companies (i) from residents (ii) for issue of shares and (iii) where such consideration (in excess of the face value of the shares) exceeds the prescribed fair market value of the shares. The difference in value determined under these provisions is taxed under the head 'Income from Other Sources' in the hands of the Company issuing shares.

As such, the provisions of Section 56(2)(viib) do not apply to investments made by non-residents and neither to investments that are made at par value. These provisions also do not apply to funds received from venture capital funds registered with SEBI (i.e., Category 1 AIF–VCF) and certain classes of persons, as notified by the Government.

There are detailed rules[1] on computation of the fair market value and they provide that the fair value is determined either by using one of the options permitted for different situations, and is based on a valuation report obtained from a Category I Merchant Banker or by substantiating the fair market value to the satisfaction of the revenue authorities, whichever is higher.

The Context

These provisions were introduced by the Finance Act, 2012, when the Hon'ble Finance Minister proposed a series of steps to deter generation and use of unaccounted money such as the introduction of compulsory reporting

1. Rule 11U, 11UA of the Income-tax Rules, 1962.

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requirements in the case of assets held abroad, permission for reopening of assessment up to 16 years in relation to assets held abroad, tax collection at source on purchase in cash or bullion or jewellery in excess of INR 2 lakhs, etc.

As per the Memorandum to the Finance Bill, 2012, Section 56(2)(viib) of the Act was also introduced under the clauses designated for setting up measures to curb the circulation of unaccounted money in the economy, along with amendments made in Section 68 of the Act. Section 68 of the Act includes provisions that seek to tax any sum credited in the books of account of taxpayers for which they cannot provide a satisfactory explanation. Such cash credits include share capital and share premiums. This provision is however not the focus of this article.

The Start-up saga

As was the case, the growth in the start-up ecosystem in India started immediately after the introduction of Section 56(2)(viib) of the Act. A new Government came to power in 2014 and decided to give the start-up ecosystem a huge impetus. In his speech on Independence Day in 2015, the Hon'ble Prime Minister introduced the 'Start-Up India, Stand Up India' scheme to promote entrepreneurship and job creation in India. Following the introduction of the programme, a Start-up India Action Plan (Action Plan) was released by the Government of India on 16th January, 2016. In a nutshell, the Action Plan envisaged the following: (i) Setting up of several incubation centres, (ii) Easy patent filing, (iii) tax exemptions, (iv) Ease in setting up business, (v) A corpus fund of INR 10,000 crores and (vi) An expedited exit mechanism.

Therefore, with hopes and aspirations pinned on the Government for the development of a world class start-up ecosystem, investors in India and abroad started pouring capital into start-ups. However, this flow of investments clashed with the anti-abuse provisions introduced by the Finance Act, 2012, leading to significant heartburn for the hapless and bootstrapped start-ups as well as their investors, who saw their capital starting to be blocked in tax litigation rather than being used for growth of their business. And while the provisions of Section 56(2)(viib) apply to all closely held companies and all resident investments, the impact was felt more by start-ups that were funded with seed capital from resident HNIs, families and friends, angel investors, etc.

Such was the outcry that over the last couple of years, the Department of Industrial Policy and Promotion (DIPP) – recently renamed the Department for Promotion of Industry and Internal Trade (DPIIT) – and the Central Board of Direct Taxes (CBDT) have needed to issue several circulars and clarifications. Indian courts have also clarified the provisions of the Act – mainly those relating to valuations.

Circulars and Notifications

The DIPP has initially issued a notification on 17th February, 2016, which considered an entity a start-up:

1. Up to five years from the date of incorporation.
2. If its turnover in any financial year did not exceed INR 25 crore.
3. If the entity was working towards innovation, development, deployment, or commercialisation of new products, processes or services driven by technology or intellectual property.

The notification also announced the constitution of an Inter-Ministerial Board of Certification for evaluating and certifying tax benefits for start-ups, since at this point, tax benefits did not include any exemption for start-ups from applicability of section 56(2)(viib).

The notification was amended by subsequent notifications dated 21st April, 2017 and 23rd May, 2017, but the circulars did not also address the issue relating to Section 56(2)(viib) faced by start-ups. Considering various representations and the implications of these provisions on start-ups, the Government finally issued a

notification on 11th April, 2018, in which its start-up policy, provided among other benefits to start-ups, exemption from applicability of Section 56(2)(viib) of the Act if they secured a specific approval from the DIPP or Inter-Ministerial Board of Certification. This was supported by a notification from the Central Board of Direct Taxes (CBDT).

While this was a positive step, the process of claiming exemption was a deterrent due to factors including the requirement for a separate approval, investor-based approval, no specified timeline for the approval to be granted, etc.

During this time, the controversy continued to build up with tax notices being issued by the Revenue authorities to start-ups, questioning them on some of their investments. The main issue on which this litigation seems to have focused was regarding valuation on which the tax office had challenged the basis of the valuation based on which shares had been issued and was of the opinion that the correct valuation should have been lower. This resulted in the tax office levying tax on the difference. As mentioned earlier, while the revenue authorities also invoked Section 68, mainly in the case of non-resident investments, in many cases, the primary controversy centred on the applicability of Section 56.

This jolted the DIPP and resulted in its taking up the matter up with the Department of Revenue. This was followed by a press release issued by the DIPP, dated 19th December, 2018, which reiterated its stand that *bona fide* investments in start-ups would be protected by the Government.

Subsequently, vide notification dated 16th January, 2019, earlier conditions pertaining to obtaining approval under Section 56(2)(viib) of the Act as provided by the notification of 11th April, 2018, were amended. While the approval process continued, it was to be granted by the CBDT and a timeline of 45 days for it to approve or reject an application was prescribed.

However, certain concerns continued to be expressed by start-up businesses regarding the applicability of these provisions (including misuse of provisions by tax authorities while making assessments on start-ups). Consequently, the DPIIT issued a fresh notification on 19th February, 2019 cancelling the previous notifications and expanding its definition of start-ups. This notification further relaxed certain provisions relating to benefits under section 56(2)(viib) of the Act. It laid down that an entity is to be considered to be a start-up:

1. Up to a period of ten years from its date of incorporation or registration, if it is incorporated as a private limited company, partnership firm or limited liability partnership firm.
2. The turnover of the entity for the any of the financial years since its incorporation has not exceeded INR 1,000 million.
3. If its work includes innovation, development or improvement of products, processes or services, or if it has a scalable business model with a high potential for employment generation or wealth creation

   (An entity formed by splitting up or reconstruction of an existing business will not be considered a start-up.)

The main conditions for exemption from applicability of 56(2)(viib) of the Act, as they stand today, are as under:

1. A company needs to be a recognised start-up according to the DPIIT's notification.
2. The aggregate amount of paid up share capital and share premium of the start-up after issue or proposed issue of share, if any, should not exceed INR 250 million rupees.
3. Furthermore, for the purpose of computing the aggregate amount of paid-up share capital and share premium of INR 250 million, the shares issued

to the following persons should not be included: (i) a non-resident, (ii) a venture capital company or a venture capital fund registered as Category I AIFs or (iii) a specified company[2].

4. Such a start-up should not have invested in certain specified assets, including shares and securities, nor made a capital contribution to another entity. These restrictions on investments are to apply to start-ups for a period of seven years from the end of the financial year in which shares are issued at premium.

A start-up fulfilling these conditions is to file a declaration in the prescribed form, stating that it fulfils the conditions mentioned above. The DPIIT will forward the declaration to the CBDT and no approval will be required for this. This change was notified by the CBDT in its circular dated 5th March, 2019.

As one would imagine, the notification above, dated 19th February, 2019, has still not eliminated some vexing issues:

1. Start-ups are not be able to make capital contribution to any other entity. The implication of this restricting factor could limit the global aspirations of start-ups intending to set up subsidiaries in other countries to conduct their business overseas.

2. The restriction on making investments in shares and securities could result in idle funds being invested in fixed deposits, and investments in securities such as mutual funds not being allowed.

On a positive note, however, the requirement for valuation has now been eliminated for start-ups. As we will discuss in the following paragraphs, current litigation has traditionally been centred around valuation, and by doing away with this requirement, much controversy should be avoided. However, it is important to note that this relaxation is only for approved start-ups, and hence, valuation-related issues will continue to be relevant for entities that are not registered as start-ups and also for past cases that are currently under litigation.

Interpretations by the Indian Tribunals on the aspect of valuations

In the context of Angel Tax, the entire discussion around valuation has become a topic of considerable debate and discussion, and certain Tribunals have had occasion to consider this issue and provide their views on the matter.

At the outset, we refer to a ruling by the Hon'ble Mumbai Tribunal in the case of M/s. Green Infra Limited (ITA No. 7762/Mum/2012) pertaining to AY 2009-10, i.e., prior to the introduction of 56(2)(viib)of the Act. In this case, the company had issued shares for a premium. It had been recently incorporated. At the time of preparation of the assessment order, the Revenue disputed the validity of charging of the share premium after looking into board minutes, internal valuation reports, submissions from respondents who were issued notices under Section 133(6) of the Act and Memorandum of Association, and considered the entire transaction a sham. The Commissioner of Income-tax (Appeals) [CIT(A)] ruled in favour of the Revenue. The Tribunal, while ruling in favour of the company, made the following observations:

- All the investors were credible, since they were directly or indirectly related to the Government.
- Charging of a premium is the prerogative of the board of directors and it is the

2. 'Specified company' means a company whose shares are frequently traded within the meaning of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and whose net worth on the last date of FY preceding the year in which the shares are issued exceeds INR 1 billion or its turnover for the FY preceding the year in which the shares are issued exceeds INR 2.5 billion.

wisdom of the shareholders whether they want to subscribe to such heavy premiums. The Revenue authorities cannot question charging of such huge premiums without there being any restriction on this from any legislated law of the land.

- It is a settled proposition of law that capital receipts, unless specifically taxed under any provisions of the Act, are excluded from income. The Hon'ble Supreme Court has laid down the rationale that share premium realised from issue of shares is capital in nature and forms a part of the share capital of a company, and therefore, cannot be taxed as revenue.

While the ruling was issued prior to the introduction of Section 56(2)(viib) of the Act and some of the observations may not hold true today, the ruling clearly indicates the approach that needs to be adopted when deciding whether a certain premium is appropriate.

There have also been certain decisions taken recently, particularly in context of Section 56. In the case of Rameshwaram Strong Glass (P) Limited (ITA No. 884/ JP/2016), the Revenue authorities had rejected the share premium amount on the ground that the company was not engaged in any business activities except for purchase of land. According to the Revenue authorities, the company lacked any credibility, goodwill or profitability, and therefore, there was no basis for the high intrinsic value of the share. The CIT(A) also rejected the valuation provided by the company. The Jaipur Tribunal, however, held that when the law provides the company with an option to use either the net asset value method or the discounted cash flow method, the Revenue authorities cannot impose a particular method on it. However, the Revenue authorities can scrutinise its valuation report, suggest necessary alterations and modifications, or even invite comment on its report by an expert. The ruling is in line with the Hon'ble Bombay High Court's ruling in the case of Vodafone M-Pesa Limited (92 Taxmann 73).

In this case, the Revenue authorities asked the taxpayer to undertake its valuation after considering its actual figures for the intervening years between the date of its valuation report and the year in which the assessment actually took place, to determine whether there was any correlation between its expected cash flow and actual cash flow. This was struck down by the Tribunal on the ground that the DCF method is based on projections (estimations) and these cannot be compared with actuals, and expect that the figures should be the same as projected.

Within a couple of months after the ruling in the case of Rameshwaram Strong Glass (P) Limited was pronounced by the Jaipur Tribunal, the Delhi Tribunal issued a ruling in the case of Stryton Exim India Private Limited (ITA 5982/Del/2018), in which the Delhi Tribunal held that variations between estimated cash flows and actual cash flows should not be so wide that the provisions of Section 56(2)(viib) of the Act become redundant. Therefore, an objective evaluation of a valuation report needs to be carried out in light of the guidelines provided by professional bodies, which need to be followed by Chartered Accountants and Merchant Bankers for valuation purposes. The matter was set aside and remanded to the files of the Revenue authorities to scrutinise evidence such as business proposals, due diligence reports, coal lease agreement, agreement for transfer of lease rights, engineering service agreement, consulting agreement, approval from environment ministry and approval from Reserve Bank of India for making overseas investments, and based on such evidence, to objectively evaluate the valuation report furnished by the assessee.

In another similar case, Innoviti Payment Solutions Private Limited (ITA No. 1278/ Bang/2018), the Bangalore Tribunal held that the most critical input of the DCF model is the cash flow projection, and therefore, such a projection should be made on the basis

of reasonable estimates arrived at by the management, and take into account various micro and macroeconomic factors affecting the business. However, the Tribunal also clarified that reasonable estimates can be made based on past data, and where such data is not available (e.g., in the case of a start-up), a reliable future estimate of cash flow should not be insisted on, but only an explanation should be sought of future expectations, based on which the valuation has been prepared. However, such expectations should be reasonable and consider various micro and macroeconomic factors.

There are some other rulings that have also held that the Revenue cannot question an entity's choice of the method of valuation or impose a different valuation method on it.

As can be seen from the above, the subject of valuation is mired in litigation and has no easy answers. And although some clarity has been provided by the rulings mentioned above, in terms of the power revenue authorities have to challenge valuation reports and cash flow projections, and in view of the hierarchical nature of the litigation process in India, this issue is unlikely to be settled soon.

Conclusion

While notifications and circulars have provided some relief to start-ups, Angel Tax is an issue faced by many companies that may not qualify as start-ups. Therefore, this issue needs to be addressed comprehensively by the Government. And while these provisions were introduced with the intention of curbing unaccounted money, their scope covers within its ambit all *bona fide* transactions as well. This has had an adverse impact on the cash flows of early stage companies because of the harsh demands, including penalties, made by tax officers and the cost of consequent litigation. This has also affected their valuations and further fund-raising activities due to the provisions required to be made by such companies.

In the case of *Vodafone International Holdings BV vs. Union of India ([2012] 341 ITR 1)*, the Supreme Court held, albeit in a different context, that valuation cannot be a basis for taxation. It also stated that valuation could be a science, but it is not law and is always a matter of opinion.

Therefore, the entire premise of levying tax, based on the fair market value being determined through valuation methodologies, needs to be reconsidered. There is a strong case for arguing that it would be better to strike off these provisions in their entirety. With the introduction of the General Anti Avoidance Rules (GAAR), the Revenue authorities in any case have the power to question the commercial rationale of a transaction to determine whether an arrangement has been undertaken with the sole intention of obtaining tax benefits.

The expectations!

While the Government has already taken various steps to ease these provisions in the case of start-ups, a lot more could still be done to further promote ease of doing business in India. And since these provisions were introduced to curb unaccounted money, they could possibly be restricted to only apply to cases where the Revenue authorities have a doubt about the genuineness of a transaction or share premium. Alternatively, the Government could consider widening the exemptions to include registered entities, pooled vehicles, accredited investors, etc.

This article is written just before the presentation of the Union Budget by the new Government. And in view of high expectations regarding the introduction of business-friendly measures in the Budget, we hope the issues mentioned above are addressed and no longer need to be debated in the future.

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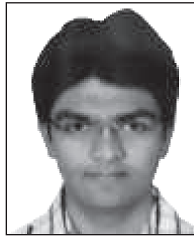

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Applicability of Section 56(2) to Transactions in Shares & Securities

Introduction

Chapter IV-F of The Income-tax Act, 1961 covers the income chargeable under the residuary head of income titled as 'Income from Other Sources'. Section 56 is the charging section of this part. Sub-section (1) of section 56 is general in nature and states that income which does not fall into any other head of income will be covered under the residuary head. However, sub-section (2) specifically provides for certain incomes/ deemed incomes which shall be considered as 'Income from Other Sources'. In this article we are attempting to analyse clause (viib) and clause (x) of sub-section (2) of section 56 as applicable to transactions in shares and securities. The valuations aspects are already covered in separate article and hence the scope of this article is restricted to the legal issues emanating from clause (viib) and clause (x) of sub-section (2) of section 56 as applicable to transactions in shares and securities.

I. Section 56(2)(viib)

1.1 Clause (viib) was inserted in section 56(2) by the Finance Act, 2012, w.e.f. 1-4-2013. (i.e., AY 2013-14). Broadly, this clause provides that when a closely held company receives from a resident person, in any previous year, any consideration for the issue of shares of the closely held company and if such consideration exceeds the face value as well as the fair market value (FMV) then the difference between the actual consideration and FMV shall be considered as income from other sources. The proviso to this clause provides for certain exceptions. Further, the Explanation to this clause gives the meaning of the term 'Fair Market Value'.

Finance Act, 2012 simultaneously amended the definition of income in section 2(24) by inserting clause (xvi) to include the excess premium amount as referred to in section 56(2)(viib) as income.

1.2 No specific reason for insertion of this clause is provided in the Explanatory Memorandum to the Finance Bill, 2012 except for classifying the amendment under the heading **"Measures to Prevent Generation and Circulation of Unaccounted Money"**. The possible objective of introducing section 56(2)(viib)

was to discourage the generation and use of unaccounted money in the guise of subscription to shares of a closely held company, at a value which is higher than the FMV of shares of such company.

1.3 **Applicability of clause (viib) of sub-section (2) of section 56**

The relevant extract from the text of clause (viib) is reproduced below:

"where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares:…."

Certain illustrations to explain the applicability of section 56(2)(viib):

Scenario No.	*Face Value per share (₹)*	*FMV per share (₹)*	*Issue Price per share (₹)*	*Applicability of clause (viib)*
1.	100	150	180	Since issue price > face value, provisions of clause (viib) are attracted. Income will be the excess of issue price over the FMV [i.e., ₹ 30 (₹ 180 - ₹ 150)]
2.	100	150	120	Since issue price > face value, provisions of clause (viib) are attracted. However nothing will be chargeable to tax because issue price is not in excess of the FMV.
3.	100	80	90	Since shares are issued at discount i.e., below the face value of shares, provisions of clause (viib) will not be attracted.
4.	100	80	110	Since issue price > face value, provisions of clause (viib) are attracted. Income will be the excess of issue price over the FMV [i.e., ₹ 30 (₹ 110 - ₹ 80)]

- The following are the important elements for the applicability of clause (viib):
  1) not being a company in which the public are substantially interested
  2) receives
  3) from any person being a resident
  4) for issue of shares
  5) amount in excess of fair market value

The above elements of clause (viib) are briefly explained below:

1.3.1 not being a company in which the public are substantially interested

This clause applies only for issue of shares of those companies wherein public are not substantially interested. Clause (18) of section 2 defines the term "company

in which the public are substantially interested" **(popularly called as widely held company).** Broadly it includes Government owned company, Banking company, company registered under section 25 of the Companies Act, 1956 (now section 8 of the Companies Act, 2013), mutual benefit finance company etc.

Thus any company which does not fall into the definition of 'company in which the public are substantially interested' will be considered as 'not being a company in which the public are substantially interested' **(popularly called as closely held company)**. This will primarily include a private limited company, an unlisted public company without majority stake held by government or statutory corporation etc. in its capital.

1.3.2 Receives

The taxable event is 'receipt' of any consideration for the Shares. The receipt of any consideration for the Shares from any person or persons, in the circumstances specified in the clause, is treated as income.

Generally, 'receive' means : to take, as something, that is offered, given, committed, sent, paid or the like; to accept. However in legal context, the term 'receive' will have a very wide meaning; it could mean anything which comes in and in the context of receipt of property, etc., it could mean receipt by means of a transfer; it could also mean receipt by means of a transfer which vests physical possession and control in the recipient.

Recently in case of *M/s. Cimex Land and Holdings Pvt. Ltd. vs. ITO [ITA No.: 5933/Del./2018],* Hon'ble Delhi ITAT held that even when the assessee received share application money in the years prior to insertion of clause (viib), but shares were allotted in AY 2015-16 [i.e., post insertion of clause (viib)], provisions of clause (viib) will be applicable and FMV needs to be determined accordingly.

With due respect to the above decision; in our humble opinion, the decision does not seem to be a correct exposition of law. Clause (viib) was inserted to curb the malpractice of routing unaccounted money through investments made in closely held companies during a particular year. Now when Finance Act, 2012 itself provides that the said clause will be applicable from A.Y. 2013-14 then the same should be strictly interpreted and all transaction for which consideration is received by the company from AY 2013-14 should only be subject to tax if contrary to clause (viib). If consideration is received in any year prior to insertion of clause (viib) and merely the allotment is made post insertion of the clause then such case must not be given retrospective effect unless specifically provided in law. As held by Hon'ble Supreme Court in *CIT vs. Vatika Township (Pvt.) Ltd. (2014) 367 ITR 466 (SC),* legislations which impose obligations or impose new duties have to be treated as prospective unless the legislative intent is clearly to give the enactment a retrospective effect.

1.3.3 from any person being a resident

This clause applies only in case where the consideration for issue of shares is received from a 'Resident'. The applicant may be any person like an individual, HUF, Company or LLP etc., however the only condition is that the subscriber to the shares of the said company must be a 'Resident'. Whether a person is 'Resident' or not will be answered by section 6 of the Act which determines the residential status of a person. In case of Individuals and HUFs, even a person who

is not ordinarily resident is considered as 'Resident' for the purpose of this clause.

This clause specifically states that it will apply only in those cases where premium is received from resident person and hence if consideration is flowing from a 'non-resident', clause (viib) will have no application. The reasonable reason to exclude the foreign remittance from this clause may be because such remittances are already regulated by RBI and FEMA law and hence the Act is not concerned with the quantum of premium charged from a non-resident person/entity.

Hon'ble ITAT Mumbai Bench in the case of *Dy. CIT vs. Finproject India (P.) Ltd. [2018] 93 taxmann.com 461 (Mum.)* observed that, to encourage foreign investments, section 56(2)(viib), r.w.s. 2(24)(xvi) of the 1961 Act is applicable to receipt towards shares from resident entities but is not applicable to the shares issued to non-residents. Further, the issue of shares at share premium by the assessee to non-resident entities was on account of capital transaction which did not have character of income chargeable to tax.

Going by the literal interpretation of section 56(2)(viib) of the Act, it appears that the residential status of the payee is relevant for the year in which the company receives the consideration for the issue of shares.

1.3.4 for issue of shares

The term 'shares' is not defined in the Income Tax Act, 1961. However, clause (84) of section 2 of the Companies Act, 2013 defines the term 'share' as : *"**share means a share in the share capita**l of a company and includes stock".*

Section 56(2)(viib) does not specify any specific class of shares to which the clause will apply. Thus, it can be inferred that issue of all classes of shares are covered by this clause i.e., equity shares or preference shares. In a recent decision of Hon'ble Kolkata ITAT in case of *M/s. Microfirm Capital Pvt. Ltd. vs. DCIT [ITA 513/KOL/2017]* it was held that section 56(2)(viib) applies to all class of shares and thus will also be applicable to redeemable non-cumulative preference shares.

Further, the clause merely states that provision will be attracted for 'issue of shares', which is a wide term and may cover various scenarios like fresh issue of shares, right issue, issue pursuant to amalgmation/merger, issue in lieu of converting debts into capital etc. However, it will not cover the case of transfer of shares by one shareholder to another as in those cases, there is no issue of shares by the company.

1.3.5 Fair Market Value

The most vital term for clause (viib) is the determination of Fair Market Value (FMV) of Shares. As per clause (a) of the Explanation to clause (viib) of section 56(2), FMV of shares will be **higher** of the following:

(i) Value as per prescribed method i.e., **in accordance with Rule 11UA(2)**

OR

(ii) Value determined by assessee using any method considering the value of assets of the company and Assessing Officer must be satisfied by such valuation.

- **Sub-Rule (2) of Rule 11UA of the Income Tax Rules, 1962**

This sub-Rule provides for two different options to assessee to determine the FMV.

Option 1: It provides for an arithmetical derivation based on the principle of Net Asset Method of valuation.

Option 2: It provides that FMV may be the value as determined by a merchant banker using the Discounted Cash Flow Method (DCF).

To summarise, the FMV for the purpose of section 56(2)(x) is **higher of the following:**

a) FMV as per Net Asset Valuation [Rule 11UA(2)(a)]

b) FMV as determined by a merchant banker as per DCF method [Rule 11UA(2)(b)]

c) FMV as may be substantiated by the company under sub-clause (ii) of clause (a) of Explanation to clause (viib).

Certain Judicial pronouncements w.r.t the method for determining the FMV

Issue: Does the assessee have the option to adopt either NAV or DCF method for valuation of shares?

- In the case of *DCIT vs. M/s. Ozoneland Agro Pvt. Ltd. (ITAT Mumbai)* [ITA No. 4854/Mum/2016 dated 2-5-2018] Hon'ble ITAT held that section 56 allows the assessee to adopt one of the methods of their choice. It is beyond the jurisdiction of the AO to insist upon a particular system, especially when the Act allows choosing one of the two methods. Until and unless the Legislature amends the provisions of the Act and prescribes only one method for valuation of the shares, the assessees are free to adopt any one of the methods.

Issue: Can Assessing Officer compare the profit projected under DCF method *vis-a-vis* actual profit of the company and reject the valuation report?

- In the case of *Rameshwaram Strong Glass (P.) Ltd. vs. ITO [2018] 172 ITD 571 (Jaipur - Trib.)*, Hon'ble ITAT held that when assessee company determined FMV of shares issued at premium on basis of DCF method in accordance with rule 11UA(2)(b) and valuation report was prepared as per guidelines given by ICAI and no fault was found in same, Assessing Officer was unjustified in changing method of valuation of shares at premium to Net Asset Value method merely because there was difference in the profits/revenues as stated in the projections used for determining value as per DCF method and the actual profits/revenue earned by the company.

Issue: Whether a heavy loss making company adopt DCF method for the valuations wherein the projections show growth and profits?

- In the case of *India Today Online (P.) Ltd. vs. ITO [2019] 176 ITD 459 (Delhi-Trib.)*, Hon'ble ITAT held that the fact that the company was loss-making does not mean that shares cannot be allotted at premium. The DCF method is a recognised method though it is not an exact science & can never be done with arithmetic precision. The fact that future projections of various factors made by applying hindsight view cannot be matched with actual performance, does not mean that the DCF method is not correct.

Issue: When can assessing officer reject the valuation made as per DCF method?

- In the case of *Innoviti Payment Solutions (P.) Ltd. vs. ITO [2019] 175 ITD 10 (Bangalore-Trib.)*, Hon'ble ITAT held that where assessee allotted shares to a company on premium and fair market value of shares was done by Chartered Accountant on basis of DCF method, only depending on information about future projections provided by management of assessee and since assessee could not conclusively establish that such projection/estimation done by its

management was on a scientific basis, Assessing Officer was justified in rejecting valuation done by Chartered Accountant.

Issue: Can Fair Market Value of Land be taken instead of book value for the purpose of determining valuation as per Rule 11UA?

- In the case o*f Minda S M Technocast (P.) Ltd. vs. ACIT [2018] 92 taxmann.com 29 (Delhi-Trib.)*, in the context of section 56(2)(viia), Hon'ble ITAT held that value of shares of a company is to be determined on the basis of book value of its assets declared in balance sheet and not as per market value of assets. However, as explained earlier, for the purpose of this clause assessee also has the option of substantiating the FMV on the basis of value of its assets as per sub-clause (ii) of clause (a) of *Explanation* to clause (viib).

Various other judicial pronouncements in the context of section 56(2)(viib)

- ***Vaani Estates Pvt. Ltd. vs. ITO [ITA 1352/Chny/2018]***

  Section 56(2)(viib) not applicable where the company had only closely related shareholders and there was no possibility of unaccounted money being involved.

  Hon'ble ITAT held that provisions of section 56(2)(viib) not applicable where there is right issue in *pari-pasu* of the existing pattern and where the company had only closely related shareholders and there was no possibility of unaccounted money being involved.

- ***ACIT vs. Enterprises Business Solutions (P.) Ltd.[2019] 104 taxmann.com 362 (Amrt.)***

  Principle of consistency
  Where assessee company had been consistently determining fair market value of shares as per DCF' method which was accepted by revenue in subsequent assessment years, Assessing Officer was unjustified in adopting 'Book Value' method in current year; addition on account of premium on issue of share, thus made, was to be deleted.

- ***Sunrise Academy of Medical Specialities (India) (P.) Ltd. vs. ITO [2018] 96 taxmann.com 43 (Kerala)***

  Interplay of section 68 and section 56(2)(viib)
  Hon'ble ITAT held that in case of a closely held company, any premium received by the said Company on issue of shares, in excess of its face value, would be treated as income from other sources as per the provisions of section 56(2)(viib) even if satisfactory explanation under section 68 is offered.

1.4 Exceptions: [Proviso to clause (viib) of section 56(2)]

Proviso to section 56(2)(viib) contains exceptions to certain class of companies form the applicability of the said clause, the said proviso is reproduced below:

Provided that this clause shall not apply where the consideration for issue of shares is received—

(i) by a venture capital undertaking from a venture capital company or a venture capital fund; or

(ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.

1.4.1 Clause (i) of the proviso exempts a venture capital undertaking from applicability of provisions of clause (viib) when consideration is received by it, for issue of its shares, form a venture capital company or a venture capital fund. It is important to note that exemption is only

in case where a venture capital company or a venture capital fund subscribes to shares of a venture capital undertaking and not on subscription by any other person/entity.

1.4.2 Clause (ii) of the proviso exempts a company from the applicability of provisions of clause (viib) when consideration is received from a class or classes of persons as notified by the Central Government. In 2016, the Government *vide* Notification No. 45/2016 dated 14-6-2016 notified start-ups to be exempted from the applicability of provisions of section 56(2)(viib) of the Act if such start-ups are recognized by the Inter-Ministerial Board of Certification under the Department of Industrial Policy and Promotion as eligible for such exemption. *Vide* notification no. 236 dated 11th April, 2018, procedure to grant of exemption to registered start-ups was provided for. Thereafter, *vide* another Notification No. GSR 364(E) dated 16th January, 2019 some amendments were made in the said procedure to make it more lucrative and time bound.

II. Section 56(2)(x)

2.1 Clause (x) of section 56(2) provides for taxability on receipt of money or certain properties without consideration or for inadequate consideration. Sub-clause (c) of clause (x) comes into application whenever any person receives in any previous year any property (other than immovable property) either without consideration or for inadequate consideration.

Explanation to clause (x) of section 56(2) refers to the *Explanation* to clause (vii) for the meaning of various terms used in clause(x). Clause (d) of the *Explanation* to clause (vii) of section 56(2) defines the term 'property' in an exhaustive manner. Therefore, any asset, howsoever valuable it is, will not be covered by the provision of section 56(2)(x), if it does not fall in one of the nine sub-clauses of clause (d) of the *Explanation* to clause (vii) of section 56(2). 'Shares & Securities' falls in sub-clause (ii) of clause (d) of the *Explanation* to clause (vii).

2.2 Summing up the above, it can be inferred that whenever any person receives 'Shares & Securities' from any person:

- without consideration and the Fair Market Value (FMV) of such shares & securities exceeds ₹ 50,000/- then whole of the value of the said shares & Securities will be chargeable as income under the head Income From Other Sources.
- for a consideration which is lower than the FMV and if the difference between the FMV and consideration exceeds ₹ 50,000/- then whole of the said difference will be chargeable as income under the head Income from Other Sources.

2.3 Issues emerging from clause (x) w.r.t. transactions in Shares & Securities

Issue: When does a person receive shares? At the time of allotment or at the time of receipt of share certificate or credit in Demat account?

- Generally a property is said to have been received when receipt of possession of the property and conferring of title are competed. On the same analogy, shares can be said to have been received only on allotment. Once the shares are allotted, shareholder is entitled

to all the rights attached to it and issue of share certificate or credit in Demat account is only a consequential step. In *Sudhir Menon HUF vs. ACIT [2014] 148 ITD 260,* Mumbai - Tribunal held that the shares are said to be received on their allotment.

Issue: Is there any chargeability u/s. 56 on issue of bonus shares or rights shares? What would be the consideration in case of issue of rights shares and bonus shares?

The transaction of bonus issue and rights issue *per se* are ostensibly covered by the clear and unambiguous language of the provision. However, does a literal application lead to any unintended or absurd results?

On allotment of bonus or rights shares, can a person be said to have 'received shares'?

- In case of a bonus issue, though, apparently nothing has been paid by the shareholder. However, one has to see that pursuant to a bonus issue only the number of shares of the shareholder increases but net value of the total shares held after bonus issue, in fact, remains the same as that before the issue of bonus shares.

The 'consideration' need not be actual inflow or outflow of money. It may be a constructive receipt. Accordingly, if receipt of one property dilutes the value of other asset, that dilution has to be considered while evaluating as to whether the consideration for the property is less than the fair market value.

In *DCIT vs. Dr. Rajan Pai [2017] 48 ITR(T) 170 - Bang. ITAT*, it has been held that an assessee who received bonus shares could never be considered as receiving something without consideration or for a consideration less than the fair market value of the property. When bonus shares are received, it is not something which has been received free or for a lesser fair market value. A consideration has flown out from the holder of the shares, may be unknown to him, which is reflected in the depression in the intrinsic value of the original shares held by him.

Mumbai Tribunal in case of *Sudhir Menon HUF vs. ACIT [2014] 148 ITD 260*, in context of bonus issue, held that the provision of 56(2)(vii) does not apply to bonus shares. It observed that –

"there is no receipt of any property by the shareholder, and what stands received by him is the split shares out of his own holding. It would be akin to somebody exchanging a one thousand rupee note for two five hundred or ten hundred rupee notes. There is, accordingly, no question of any gift of or accretion to property; the shareholder getting only the value of his existing shares, which stands reduced to the same extent."

The Tribunal, on the issue of applicability of this provision to the rights issue, observed as under:

- In a pro-rata allotment of shares in proportion to existing shareholding of the shareholders, there is only an apportionment of the value of their existing holding over a larger number of shares.
- A higher than proportionate or a non-uniform allotment would attract the rigour of the provision. This is only understandable in as much as the same would only be to the extent of the disproportionate allotment and, further, by suitably factoring in the decline in the value of the existing holding.
- In the case of issue of bonus shares (as also on demerger), no property is being conveyed to the shareholder in as much as the property therein is comprised in the existing shareholding of the allottee. There is as such no case of a gift; the shareholder

only receiving his own property, albeit in a different form.

- In case of right shares, to the extent it is allotted to a person not against his existing shareholding or, even so, albeit disproportionately, there is scope for value or property being passed on to him, depending on the terms of the allotment, which cannot be said to be in lieu of or as recompense of his existing property.

Disproportionate rights issue theory in *Sudhir Menon HUF vs. ACIT [2014] 148 ITD 260(Mum)*, with respect, travels on the circumference not going to the root of the provision. Undoubtedly, the provision is introduced to counter money laundering and bogus capital building and to bring back the gift tax regime only in a new form keeping the same substance. In the context of Gift Tax Act, Supreme Court in *Khoday Distilleries Ltd. vs. CIT and Anr. [(2008) 307 ITR 312]* held that 'allotment of shares' does not involve transfer. Can there be a receipt in the hands of shareholder, without there being transfer in the hands of the company? A purposive interpretation of section 56(2) will suggest that these provisions are not intended to apply to rights issue.

It is worth to make reference to three circulars issued by CBDT recently in quick succession.

1) Circular No. 10/2018, dated 31st December, 2018:

"It is apparent from the legislative intent that clause (viia) was inserted in section 56(2) of the Act as an anti-abuse provision to prevent the practice of transferring shares of a specified company for no or inadequate consideration. Thus, the intention was never to apply these provisions of said clause (viia) to the fresh issuance of shares as mentioned in para 2 above, by the specified company. Keeping in view the legislative intent to apply anti-abuse provision contained in section 56(2)(viia) to transfer of shares for no or inadequate consideration, it is hereby clarified that section 56(2)(viia) of the Act shall apply in cases where a specified company or firm receives the shares of the specified company through transfer for no or inadequate consideration. Hence, the provisions of section 56(2)(viia) of the Act shall not be applicable in cases of receipt of shares by the specified company or firm as a result of fresh issuance of shares as mentioned in para 2 above, by the specified company."

2) Circular No. 02/2019 [F. No. 173/616/2018-ITA-I], dated 4-1-2019

"…….Given the fact that the matter relating to interpretation of the term 'receives' used in section 56(2)(viia) of the Act is pending before judicial forums and stakeholders have sought clarifications on similar provisions in section 56 of the Act, the Board is of the view that the matter is required to be examined afresh so that a comprehensive circular on the matter can be issued……

4. In view of the above, the Circular No. 10/2018 dated 31st December, 2018 issued from file No. 173/616/2018-ITA-I is hereby withdrawn and the aid circular shall be considered to have been never issued."

3) Circular No. 3/2019 [F. No. 173/616/2018-ITA.I], dated 21-1-2019

"……Keeping in view the plain reading as well as the legislative intent of section 56(2)(viia) and similar provisions contained in section 56(2) of the Act, being anti-abuse in nature, it has been decided that the view, as was taken in Circular No. 10/2018 [subsequently withdrawn by Circular No. 02/2019] that section 56(2)(viia) of the Act would not apply to fresh issuance of shares, would not be a correct approach, as it could be subject to abuse and would be contrary to the express provisions and the legislative intent

of section 56(2)(viia) or similar provisions contained in section 56(2) of the Act.

3. *Therefore, any view expressed by the Board in Circular No. 10/2018 shall be considered to have never been expressed and accordingly, the said circular shall not be taken into account by any Income-tax authority in any proceedings under the Act….."*

Circular No. 10/2018 dated 31st December 2018, though withdrawn subsequently, also answers the question.

To strike a balance, we may say that where, however a case of bogus capital building *via* rights issue is established by the revenue, the disproportionate rights issue theory may be upheld. But where there is no such proof of manipulations, a mere disproportionate rights issue should not trigger the provision of section 56(2)(x).

Issue: Is buyback of shares at less than FMV taxable in the hands of the company undertaking the buy-back?

- Sub-section (7) of section 68 of the Companies Act, 2013 mandates the company to extinguish and physically destroy the shares or securities bought back within seven days of the last date of completion of buy-back. Hence, it is clear that a company cannot 'hold' its own shares or securities.

In case of *Vora Financial Services (P.) Ltd. vs. ACIT [2018] 96 taxmann.com 88 (Mumbai-Trib.),* Hon'ble Tribunal in context of section 56(2)(viia) observed that section 56(2)(viia) should be applicable only in cases where the receipt of shares become property in the hands of recipient and the shares shall become property of the recipient only if it is "shares of any other company". Accordingly it may be inferred that such transaction would not fall under the ambit of taxability u/s. 56(2)(x).

Reference can be made to decision of Hon'ble Supreme Court in case of *CTO vs. State Bank of India (Civil Appeal No. 1798 of 2005).*

2.4 Exceptions for certain genuine transactions

The proviso to clause (x) contemplates certain genuine transactions and excludes the same from the tax net. Thus when shares or securities are received from any person referred to in the exceptions then such transaction would not be subject to tax. The exceptions are discussed briefly as under:

I. from any relative;

Certain Judicial Pronouncements

Recently, in *Subodh Gupta (HUF) vs. PCIT [2018] 169 ITD 60 (Delhi ITAT)*, it was held that, receipt by an HUF from Karta's mother is not covered by the definition of 'relative'. Reason being that mother of Karta is not a member of Karta's HUF. With due respect, this judgment appears to be not a rational one as it is simply going by the rule of literal interpretation. Certainly, the objective behind these provisions is to counter money laundering and bogus capital building. Taxing gift by Karta's mother to Karta's HUF is an over stretching on the literal interpretation of the term.

In *Kumar Pappu Singh vs. DCIT [2019] 101 taxmann.com 122,* the assessee received rights shares in excess of the proportionate ratio for consideration less than fair market value from a company in which all the shareholders were his close relatives, each of them fell in the definition of 'relative'. The Visakhapatnam ITAT, considering the provisions as anti abuse measure, held that surrender of the rights of the close relatives in favour of another close relative is covered by exemption under section 56(2)(vii)(c). However, contrary view can be found in *Gyanchand M. Bardia vs. ITO [2018] 93 taxmann.com 144 (Ahmedabad-Trib.).*

II. on the occasion of the marriage of the individual; or

III. under a will or by way of inheritance; or

IV. in contemplation of death of the payer or donor, as the case may be; or

V. from any local authority as defined in the Explanation to clause (20) of section 10; or

VI. from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or

VII. from or by any trust or institution registered under section 12A or section 12AA; or

VIII. by any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of section 10; or

IX. by way of transaction not regarded as transfer under clause (i) or 85 [clause (iv) or clause (v) or] clause (vi) or clause (via) or clause (viaa) or clause (vib) or clause (vic) or clause (vica) or clause (vicb) or clause (vid) or clause (vii) of section 47; or

X. from an individual by a trust created or established solely for the benefit of relative of the individual.

III. Reference to Valuation Officer w.r.t. clause (viib) and (x) of section 56(2)

a) Unlike sec 50C, neither this Rule nor section 56(2)(viib) or (x) provides for making any reference to Valuation Officer.

The opening words of section 55A, *"With a view to ascertaining the fair market value of a capital asset for the purposes of this Chapter.."* may not support such reference to Valuation Officer in case of section 56(2)(viib) or (x) as it falls in Chapter IV-F.

b) In *Jindal Srips Ltd. vs. ITO [1979] 116 ITR 825 (Punj. &Har.)(FB)* and in *CIT vs. Dr. C. Ashokan Nambiar [200] 245 ITR 37 (Ker.)*, it was held that when no question of determining capital gains is involved, reference to sec 55A would be improper. In *CIT vs. Smt. Nilofer I. Singh [2009] 176 Taxmann 252 (Delhi)* it was held that reference to a Valuation Officer under section 55A is for object of ascertaining fair market value of a capital asset and it is only when Assessing Officer is required to ascertain fair market value of a capital asset that provisions of section 55A can be invoked.

c) The plea that except for the purpose of capital gains and for no other purpose sec 55A could be availed of, cannot conform to either the language or the object of the said provision or to reason or logic – *C.T. Laxmandas vs. Asst. CIT [1994] 208 ITR 859 (Mad.)/CIT vs. Smt. Basana Rani Saha [2000] 111 Taxman 712 (Gau.)/Om Prakash Bamba vs. Valuation Officer 2001 Tax LR 157 (J&K).*

d) However, subsequently, this controversy seems to have rested by Supreme Court in *Smt. Amiya Bala Paul vs. CIT [2003] 130 Taxman 511 (SC)* where it held that -

"Section 55A having expressly set out the circumstances under which and the purposes for which a reference could be made to a Valuation Officer, there is no question of the Assessing Officer invoking the general powers of enquiry to make a reference in different circumstances and for other purposes. It is noteworthy that section 55A was introduced in the Act by the Taxation Laws (Amendment) Act, 1972 when sections 131(1), 133(6) and 142(2) were already on the statute book. If the power to refer any dispute to a

Valuation Officer was already available in sections 131(1), 133(6) and 142(2), there was no need to specifically empower the Assessing Officer to do so in certain circumstances under section 55A. A Valuation Officer appointed under the Wealth-Tax Act can discharge functions within the statutory limits under which he is appointed. It is not open to a Valuation Officer to act in his capacity as Valuation Officer otherwise than in discharge of his statutory functions. He cannot be called upon nor would he have the jurisdiction to give a report to the Assessing Officer under the Income-tax Act except when a reference is made under and in terms of section 55A or to a competent authority except under section 269L."

e) Thereafter section 142A was inserted in the Act *vide* Finance (No. 2) Act, 2004 with retrospective effect from 15-11-1972 to provide for reference to Valuation Officer for the purpose of section 69, section 69A and section 69B. *Vide* Finance Act 2010, the said section was amended w.e.f. 1-7-2010 so as to provide for reference to Valuation Officer for the purpose of section 56(2) also. But in *Sargam Cinema vs. CIT (2010) 328 ITR 513 (SC)*, it was held that no such reference can be made to a Valuation Officer by the Assessing Officer without rejecting the books of account. To nullify the effect of this judgment, section 142A was substituted by the Finance (No. 2) Act, 2014 w.e.f. 1-10-2014 to provide that *"The Assessing Officer may make a reference to the Valuation Officer under sub-section (1) whether or not he is satisfied about the correctness or completeness of the accounts of the assessee."*

However, with that substitution, the reference to section 69, section 69A and section 69B in sub-section (1) has been done away with. Sub-section (1) in the substituted section 142A has been generally worded and the phrase "where an estimate of the value of any investment referred to in section 69 or section 69B or the value of any bullion, jewellery or other valuable article referred to in section 69A or section 69B or fair market value of any property referred to in sub-section (2) of section 56 is required to be made" do not find a place therein. Therefore, in the author's opinion, section 142A is wide enough to enable an Assessing Officer to make a reference to Valuation Officer in all cases where a dispute arises as to the interpretation of Rule 11UA. Further the use of the word 'may' in section 142A should not be interpreted in a restrictive or discretionary sense. In the context of section 50C(2), in several cases, Tribunal has held that the word 'may' should be interpreted as 'shall'.

f) A question then arises as to the scope of powers of Valuation Officer as to whether he can deviate from the Valuation Rules 11U and 11UA and use any other formula. In the context of Wealth-Tax Act, Supreme Court in *Bharat Hari Singhania vs. CWT [1994]73 Taxman 3*, has held that the Valuation Officer is a creature of the statute. He is, therefore, bound by the provisions of the statute and the rules made thereunder unless there is something either in the Act or in the rules to indicate otherwise.

IV. Conclusion

Ostensibly the simple provision of Chapter IV-F of the Income-tax Act, 1961 (being a residuary head) contains certain provisions which are really complicated and litigative in nature. The article attempts to touch certain areas of section 56(2)(viib) and 56(2)(x) as applicable to transaction in shares and securities. However, it is quite possible that there may be many other issues emerging from the two clauses but not comprehended by the authors. After all, "to err is human".

❍❑❍

CA Kinjal Shah & CA Dhaval Vakharia

Fixed Income Securities (Listed & Unlisted) – Accounting & Auditing

A. Introduction

The Indian retail investor has predominantly been risk averse and preferred investing in assured fixed income instruments like Bank Deposits, Small Saving Schemes, insurance Policies etc. and in physical assets like gold, real estate etc. Over a period of time, there has been a significant shift in investment patterns of retail and HNI investors from physical assets to financial assets, which got further accentuated in the post demonetisation period.

A lot of avenues are now being made available to Retail, HNI and Corporate investors for better asset allocation and to generate efficient risk-adjusted return including Fixed Income Instruments.

Before we discuss the accounting and auditing aspects of Fixed Income Securities, let us examine the definition of securities, as defined in Section 2(81) of the Companies Act, 2013 to mean 'securities' as defined in Section 2(h) of the Securities Contracts (Regulation) Act, 1956 (SCRA). Although SCRA regulates only the listed entities, the definition of the term securities under SCRA also applies to The Companies Act due to such cross referencing.

Section 2(h) of SCRA: 'Securities' include the following:

- Shares, scrips, stocks, bonds, debentures, debenture stocks etc. in or of any incorporated company or another body corporate.
- Derivatives.
- Units issued by any Collective Investment Scheme to the investors in such scheme.
- Security receipt as defined in Section 2(zg) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
- Units or any other such instruments issued to the investors under any Mutual fund scheme.
- Government Securities.
- Such other instruments, rights or interest therein shall be declared by the government to be securities.

[1]"Fixed Income" refers to any type of investment under which the borrower or issuer is obliged to make payments of a fixed amount on a fixed schedule. For example, the borrower may have to pay interest at a fixed rate, say once a year, and to repay the principal amount on maturity. Fixed income securities can be contrasted with equity securities – often referred to as stocks and shares – that create no obligation to pay dividends or any other form of income at a pre-agreed interval.

The term 'fixed' in 'fixed income' is also applied to a person's income that does not vary materially over time and can be distinguished from inflation-indexed bonds, variable-interest rate instruments, and the like.

Hence, the term Fixed Income Securities means the instruments which assures fixed income and is defined as securities under SCRA. Such Fixed Income Securities could be listed on the recognised stock exchange or could be traded over the counter (OTC) or possibly may not have any market for price discovery at all unless bought back or redeemed by the issuer. We shall primarily focus the discussion around Fixed Income Securities which includes:

1. Bonds including perpetual bonds, corporate bonds, deep discount bonds, zero coupon bonds
2. Debentures – Convertible debenture, Non-convertible debenture (NCD), secured, unsecured etc.
3. G-Sec/T-Bills issued by State/Central Government.
4. Money Market Instruments
5. Units of Mutual funds – Liquid Fund, Fixed Income Plan, Debt Fund, Fixed Maturity Plan, Gilt Fund, Monthly Income Plan etc.

B. Types of Fixed Income Instruments

Let us briefly understand key debt products (Fixed Income Instruments):

1. Fixed Deposit Receipt ('FD')

In India, Fixed Deposits (FDs) are the most popular fixed-income instrument to generate steady income. Fixed Deposits are usually of two kinds, Bank Fixed Deposits and Company Deposits. Fixed deposits placed by investors with companies for a fixed tenure at a pre-determined rate are called Company Deposit and they work similar to Bank Deposits.

2. Debentures

Debenture is a debt instrument, normally issued by a company, yielding a fixed rate of interest to the investors, as per the agreed terms. The debentures could be secured or unsecured. Further, it could be convertible, partly convertible or non-convertible. Normally, the rights of investors and obligations of the issuer are provided in the 'terms of issue' of debentures.

3. G-Sec

A government security (G-Sec) is a debt obligation of the Indian Government to fund the Government expenditures. These instruments are tradable and are issued either by the Central or the State Government. These securities are offered for short term as well as long term. The

1. *Source*: Wikipedia.

yield of 10-year G-Sec bond, issued by the Central Government is considered as the benchmark yield in India.

4. **Bond**
A bond is an obligation or loan, normally issued by a Government or a company and subscribed by investors. In turn, the issuer promises to repay the principal (or face value) of the bond on a fixed maturity date to make regularly scheduled interest payments. The major issuers of bonds are governments and corporations.

5. **Treasury bills ('T-Bills')**
The Government bodies like Municipal Corporations or State Government, usually issue Treasury Bills, commonly known as T-bills, to raise money from the investors. These are basically similar to bonds, but with a maturity up to 364 days. T-bills usually don't pay regular interest payments. They are typically sold below par and the difference between the face value and price of a T-bill becomes the interest payment.

6. **Commercial Papers**
Commercial paper is a short term debt instrument, usually issued by corporates to finance its working capital requirements. Normally, it is an unsecured money market instrument, issued in the form of a promissory note, and is issued below par up to 364 days of maturity.

7. **Debt Mutual Fund**
Debt Mutual Funds collects funds from investors, mainly to invest in a mix of debt or fixed income securities such as T-Bills, G-Sec, Corporate Bonds, Money Market instruments and other debt securities of different time horizons. The basic reason behind investing in debt fund is to earn fixed income and capital appreciation. Liquid Mutual Fund, Fixed Income Plan or Monthly Income Plan are nothing but a variant of debt mutual fund, with differentiated and specific investment objectives to be achieved.

8. **Fixed Maturity Plan ('FMP')**
FMPs are closed-end debt mutual funds having a fixed maturity period. Unlike other open-ended debt funds, FMPs are not available for subscription on a continuous basis. Usually, FMPs invest only in Fixed Income Instruments whose duration is similar to its own term to align its term with that of its underlying assets. Such alignment is done to eliminate the impact of risk of interest rate fluctuation to generate stable return from a debt investment. Needless to mention that the credit risk of the underlying portfolio in an FMP remains another key variable while selecting the same.

9. **Perpetual Bond**
A perpetual bond is a bond without a maturity date. However, the issuer has an option to buy back the bond after a specific period (known as 'Call Option' or 'Call Date'). In India, perpetual bonds are listed exchange and are freely tradable. An investor can sell/purchase the bonds on the exchange and thus providing liquidity to the investors. These bonds are generally issued by large manufacturing companies or by banks to fund their long-term capital requirements.

Out of the aforesaid Fixed Income instruments, FDs and CPs are not covered under the definition of 'security' under the provisions of SCRA.

C. Accounting aspects of Fixed Income securities

The accounting aspects would broadly be governed by the respective standards applicable to the entity/investor.

- IND-AS 107 & 109 shall be applicable to listed companies (excluding companies listed on SME Exchanges), holding/subsidiary/joint venture/associate of listed companies, Private companies with net-worth exceeding ₹ 250 crores, Insurance companies and NBFCs.
- Accounting Standard 13 shall be applicable to all other companies (other than mentioned above).
- All other entities to follow accounting practice as per generally accepted accounting practices.

In this article, we have covered the accounting and auditing aspects of Fixed Income securities, from the perspective of an Investor (and not from issuer's perspective). Further, this article covers accounting and auditing aspects as covered under AS-13 – 'Accounting for Investments' and does not deal with Ind AS (new standards in line with IFRS).

1) Introduction & definition

AS-13 deals with accounting for investments in the financial statements of enterprises and related disclosure requirements.

It is pertinent to note that AS-13 does not apply to mutual funds, venture capital funds, related asset management companies, bank and public financial institution formed under Central or State Government Act or as defined in the Companies Act, investments of retirement benefit plans and life insurance enterprises.

As per footnote to para 1, AS-13, to the extent it relates to current investments, shall also apply to shares, debentures and other securities held as stock in trade with suitable modification.

Further, under AS-13, the term 'Fair Value' is defined to mean the amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction. Under appropriate circumstances, market value or net realisable value provides an evidence of fair value.

Some of the Fixed Income instruments, like NCDs, G-Sec, Perpetual Bonds, etc. are listed on the stock exchange or a liquid market exists from which a market value can be established. For such investments, market value generally provides the best evidence of fair value. For other investments, where an active market do not exist, other means are used to determine the fair value.

2) Classification of investment

While enterprises present financial statements that classify fixed assets, investments and current assets into separate categories, AS-13 classifies an investment into two broad categories:

a) 'Current Investment' – which is defined to mean an investment that is by its nature readily realisable and is intended to be held for not more than one year from the date on which such investment is made. Such Current Investment can form part of the investments or it can be shown as stock-in-trade under the head 'current assets' in the balance sheet.

b) 'Long Term Investment' which is defined to mean an investment other than Current Investment, even though they may be readily marketable.

3) Cost of Investments

As per AS-13, the cost of an investment includes acquisition charges such as brokerage, fees, duties, etc. In case investment is acquired or partly acquired, by issue of another security, the acquisition cost is the fair value of the security issued. Similarly, when investment is acquired in exchange for another asset, fair value of asset given up shall be considered as an acquisition cost.

AS-13 also provides for adjustment to the cost for accrued interest on Fixed Income securities, earned up to the date of acquisition. Interest received subsequent to the acquisition of Fixed Income security is allocated between pre-acquisition and post-acquisition periods; the pre-acquisition portion is deducted from cost of investments.

Illustration

A Ltd bought NCD of Z Ltd.

Coupon rate – 10% payable annually

Purchase Price – ₹ 106

Brokerage & other charges – ₹ 2

Face value (FV) – ₹ 100

Purchase date – 30-Sep

Answer

The initial cost of asset shall be ₹ 108 (106+Brokerage of ₹ 2).Subsequently, when interest of ₹ 10 (for the 12 months) is received on March 31 it should be segregated between pre-acquisition and post-acquisition interest.

Pre-acquisition interest of ₹ 5 for 6 months till 30-Sep (₹ 100 FV x 10% x 6/12) shall be reduced from the cost of NCD and carrying value of NCD shall be ₹ 103.

Illustration

A Ltd. acquires Bonds worth ₹ 10 Lacs, incurs ₹ 25,000 towards brokerage and ₹ 30,000 towards government duties (Stamp duty). Subsequently after 1 month A Ltd. incurs legal cost of ₹ 50,000 due to dispute with seller. Ascertain the cost of the investment.

Answer:

Cost of Investment shall be ₹ 10.55 lakhs (inclusive of Brokerage and government duties). However legal cost incurred subsequently cannot be included in cost of investment. (***Note***: In case of investment in equity shares the standard requires STT also to be forming part of cost irrespective of tax treatment).

4) Carrying Amount of Investments

As per AS-13, the carrying amount for Current Investment shall be at lower of cost and Fair Value. Any reduction in fair value as well as any subsequent reversals are included in the profit and loss statement.

For Long Term Investment, carrying amount is usually at cost. However, if there is any decrease in the Fair Value, barring temporary one, the resultant reduction in carrying amount is required to be charged to the profit and loss statement. Further, when there is rise in the value of investment, the aforesaid reduction in the carrying amount is reversed.

AS-13 provides that valuation of Current Investments on overall basis is not considered appropriate. Further, Long-Term Investments are usually of individual importance to the investing enterprise. The carrying amount of Long-Term Investments is therefore determined on an individual investment basis.

Illustration

(in ₹)

Sr. No.	Investment	Cost	Market Value
1.	In Mutual Funds		
	A	50,000	48,000
	B	10,000	15,000
	Side pocket units of A	0	3,000
	Sub-total of (1)	60,000	66,000
2.	In G-Sec		
	A	80,000	88,000
	B	100,000	98,000
	Sub-total of (2)	180,000	186,000
	TOTAL	240,000	247,000

Compute the carrying amount of investment considering it to be – Option 1: Long-term investment & Option-2: Current investment.

Note: Mutual fund A has segregated 10% of its portfolio into side pocket units.

Answer

SEBI has permitted debt mutual fund schemes in India to create side pockets for stressed assets. Under such situation, the normal units will continue to be available for regular redemption but side pocket units will be redeemed only when the AMC is able to liquidate/realise its investment.

Option-1: Long-term investment

The company will have to provide for the permanent reduction in carrying value in the units of Mutual Fund A for ₹ 2,000. Since all other decline will be considered temporary in nature, no additional provision would be required in the carrying value of investments (AS-13 do not permit valuing long term investment on global or category-wise level).

Note: Alternatively, if the company had opted to account side pocket units of A at a cost of ₹ 5,000 (considering it represents 10% of the total portfolio) and correspondingly reducing the cost of normal units as under:

(in ₹)

Sr. No.	Investment	Cost	Market Value
1.	In Mutual Funds		
	A	45,000	48,000
	B	10,000	15,000
	Side pocket units of A	5,000	3,000
	Sub-total of (1)	60,000	66,000

In such case there will not be any provision on units of A, but side pocket units will warrant provision of ₹ 2,000; considering the market value to be ₹ 3,000.

Further considering the fact that underlying assets of side pocket units are stressed assets, which may not be realisable in near future and will also have an impact on the cash flow arising from such investments; it shall be prudent to make provision of ₹ 5,000 being cost of side pocket units.

Option-2: Current investment
The company has option to value the investment at individual level requiring a provision of ₹. 4,000 (₹ 2000 for Mutual Fund A + ₹ 2,000 for G-Sec B) or to value investment category-wise, requiring no adjustments to carrying value . Further, AS-13 provides that valuation of current investments on overall basis is not considered appropriate. Side pocket units would not warrant provisioning since they are accounted at Zero cost in the books.

5) **Disposal of Investments**
AS-13 provides that on disposal of an investment, the difference between the carrying amount and the disposal proceeds, net of expenses, is recognised in the profit and loss statement.

Further, while disposing of a part of the holding of an individual investment, the carrying amount to be allocated to the part being sold, is to be determined on the basis of the average carrying amount of the total holding of the investment. In respect of shares, debentures and other securities held as stock-in-trade, the cost of stocks disposed of is determined by applying an appropriate cost formula (e.g., first-in, first-out; average cost, etc.)

6) **Reclassification of Investments**
AS-13 provides following principles measurement and recognition in case of reclassification of investments:

a) Long-term Investments reclassified as Current Investments – at lower of cost and carrying amount as on the date of transfer;

b) Current Investments reclassified as Long-term Investments – transfers are made lower of cost and Fair Value as on the date of transfer.

However, AS-13 does not provide any condition precedents for reclassification of investment from Long Term to Current or *vice-versa*.

Illustration
A Ltd. invested ₹ 1 crore in NCD in Jan-17 with maturity in Jan-20. The investment was classified as long-term at the time of initial investment. Whether the company should re-classify its investment as on Mar-19 from Long term to current investment considering that the period to maturity as on Mar-19 is less than one year.

Answer:
Classification of investment is determined on the date on which the investment is made and hence the classification would continue to remain long-term as on Mar-19.

7) **Disclosure**
As per AS-13, various disclosures are required. The key disclosures being:

a) Appropriate accounting policy to determine carrying amount.

b) Separate disclosure of income from each type of investments i.e., Long-Term and Current Investments.

c) Significant restriction of the right of ownership, reliability of investments or the remittance of income and proceeds of disposal.

d) The aggregate amount of quoted and unquoted investments, with market value of quoted investments.

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D. [2]Audit of Fixed Income securities

Some important aspects in audit of investment in general and investment in fixed income securities in specific have been enumerated hereunder:

1) **Internal Control Evaluation**

Evaluate the system of internal control relating to investments to determine the nature, timing and extent of audit procedures.

(a) Control over acquisition, accretion and disposal of investments: Verify proper authority for sanction, acquisition and disposal of investments are made in accordance with the legal requirements governing the entity as well its internal regulations like the articles of association, rules and regulations, trust deed, etc.

(b) Safeguarding of investments: Verify that the investments are in the name of the entity, existence of proper system for the safe custody of all securities or other documents of title to the investments belonging to the entity.

(c) Controls relating to title to investments: Ensured that in cases where the title is transferred to the entity in due course of time, benefits accruing since the acquisition are properly accounted and recovered.

(d) Information controls: These controls should ensure that reliable information is available, along with proper documentation, for recording acquisitions (including by way of conversion of securities, right issues or other entitlements, under schemes of amalgamation, acquisition, etc.), accretions and disposals, and for ascertaining the market values etc.

2) **Verification of transaction**

Verify that transactions for the purchase/sale of investments are supported by due authority and documentation. Transaction should also be verified with reference to the broker's contract note and other similar evidence. In case where investments have been purchased or sold cum-interest/ex-interest verify whether proper adjustments in this regard have been made in the cost/sales value of securities purchased or sold. In case of over the counter or off-market purchase/sale transaction auditor may verify the price at which the transaction is executed *vis-à-vis* the prevailing market price and in case of material variance, auditor should satisfy himself as regards the genuineness of transactions.

3) **Physical verification**

Securities can either be held in Dematerialised form or physical form. In case of physical securities extra caution is required to be exercised since exchanges have discontinued trading of such securities as per recent SEBI directives. Auditor should enquire the reason for holding securities in physical form and ensure that the entity continues to remain the beneficial owner of such securities by obtaining external confirmations from the Issuer/RTA (Registrar and Transfer Agent) of the securities. A confirmation

2. *Reference*: Guidance note of ICAI on Audit of Investments.

from RTA may also be obtained as regards the address and bank details as per their record for communication and payment of corporate action/other benefits. In case of G-sec held in physical form, a confirmation should be obtained from the public debt office of the RBI.

In case of demat securities, the auditor should obtain a certified copy of the 'Transaction-cum-Holding Statement' of the demat accounts where such securities are held. Auditor should preferably insist that such confirmations are mailed directly by the depository to the auditor in a sealed envelope. Auditor should also verify that there exist a process of periodic reconciliation of securities and differences, if any as per books and demat statement are resolved.

Auditor should obtain confirmation as regards existence of securities as on Balance Sheet date where the shares are held by third party (like custodian, Brokers, Banks etc.). The auditor should obtain justification for custody of securities with third parties.

In case where the shares are held in the name of Director in case of Companies, Trustees/nominees in case of trust or Partners in case of firm, the auditor should ascertain the reasons for the same and examine the relevant documentary evidence (e.g., written confirmations) supporting the real/beneficial interest of the entity in the investments.

The auditor should also examine any other aspects required to be examined or reported upon by the relevant statute.

4) **Examination of Valuation and Disclosure**
Verify that the investments have been valued and disclosed in the financial statements in accordance with recognised accounting policies and practices and relevant statutory requirements like Companies Act, Indian Trust Act, Co-operative Societies Act, Accounting Standard 13 on Investment etc., as applicable to the entity. Verify that method of valuation followed by the entity is consistently applied.

Ensure that the expenditure incurred on account of transfer fees, stamp duty, brokerage, etc., is included in the cost of investments. Auditor may ascertain the carrying value of quoted investment with the closing price on stock exchange. In case of unquoted investment special care should be taken to verify the method of valuation adopted by the entity and impairment, if any.

5) **Analytical Review Procedure**
To judge the overall reasonableness of the amounts of investments in fixed interest-bearing securities the auditor may relate the amount of interest earned with the face value of the related securities and compare this ratio with the similar ratio for the previous years. This ratio could as well be compared to the interest prevailing during the corresponding audit period.

6) **Management Representation and Documentation**
The auditor should obtain a Management Representation (MR) from the management of the entity regarding classification and valuation of investments for Balance Sheet purposes.

The auditor should ensure maintenance of adequate working papers regarding audit of investments.

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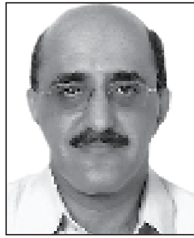

CA Zubin F. Billimoria

Measurement and Disclosure in Financial Statements – Shares (Listed & Unlisted)

Introduction

Companies invest in shares for various reasons depending upon the sector in which they are operating or their strategic and business objectives. Accordingly, the investments may be made to earn returns by deployment of temporary surplus, to earn regular income by way of dividends or for strategic purposes in group companies. The purpose of this article is to examine the various aspects dealing with the accounting (which primarily covers the measurement and disclosure aspects) around investments in shares, both listed and unlisted.

Measurement Aspects

The measurement and the corresponding accounting treatment for shares depends upon whether the entity needs to follow the normal accounting standards (erstwhile Indian GAAP) or the Indian Accounting Standards (Ind AS), which correspond to the global International Financial Reporting Standards (IFRS).

Let us now proceed to analyse the measurement and related accounting aspects both under Indian GAAP and Ind AS.

Indian GAAP

The measurement aspects under Indian GAAP are relatively straight forward and are codified in **Accounting Standard 13 (AS-13)** which deals with the *accounting treatment for all types of investments, unlike in the case of Ind AS, as discussed subsequently, where there are specific requirements dealing with investments in shares, depending upon whether they are in the nature of debt or equity. Hence our* ***subsequent discussion in AS-13 though referring to the term investments would need to be understood in the context of shares.*** The key requirements laid down thereunder are as under:

Classification

The measurement and the corresponding accounting treatment under AS-13 is primarily driven by the classification of the investments. The key principles in respect thereof are as under:

- All investments are required to be classified either as **current investments** or **long term investments**.

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- A **current investment** is one that by its nature is **readily realisable** and is **not intended** to be held for more than one year from the date of its acquisition. The important point which needs to be noted that the classification is ***not merely dependent upon the period of holding but also upon the purpose and intention and hence it is imperative that the same is clearly identified at the point of acquisition*** since the measurement and the accounting treatment is dependent thereupon.
- The above classification is to be made for each individual investment. The Standard does permit reclassification though the same is expected to be few and far between.
- Any investment which does not meet the definition of a current investment is regarded as a long term investment.

Apart from the above broad principles, there is very limited guidance given in AS-13 regarding the classification and hence it is important for companies to frame an appropriate policy, especially where the volume of transactions is significant.

Carrying Value

As discussed above, the classification of the investments determines their carrying value and subsequent measurement. The key principles in respect thereof are separately discussed for long term and current investments.

Long Term Investments

The broad principles dealing with the measurement of long term investments are as under:

- All long term investments are initially required to be carried at cost, which includes acquisition charges such as fees, brokerage and other statutory levies.
- If an investment is acquired, or partly acquired, by the issue of shares or other securities, the acquisition cost is the fair value of the securities issued (which, in appropriate cases, may be indicated by the issue price as determined by statutory authorities). The fair value may not necessarily be equal to the nominal or par value of the securities issued.
- If an investment is acquired in exchange, or part exchange, for another asset, the acquisition cost of the investment is determined by reference to the fair value of the asset given up. It may be appropriate to consider the fair value of the investment acquired if it is more clearly evident.
- In the subsequent periods, the initial acquisition cost can be continued as the carrying value, unless there is a ***decline other than temporary in the value of the investment,*** in which case the same needs to be recognised.
- The decline in the carrying amount, if any, determined above is required to be charged off to the profit and loss account. The reduction in the carrying amount is reversed when there is a rise in the value of the investment or the reasons for the reduction no longer exist.
- The carrying amount needs to be determined on an individual basis.

The Standard has specified that the following are some of the indicators of the value of an investment which need to be analysed to determine the continued relevance of the initial carrying cost:

a) The market value in case it is quoted.

b) The investee's net assets.

c) The operating and financial results and cash flows of the investee.

d) The type and extent of the investors stake in the investee.

e) Restrictions on distributions by the investee or on the disposal by the investor.

Accordingly, it is imperative that the company has a proper mechanism for monitoring the above triggers for all significant long term investments in shares so as to identify on a timely basis any decline in the value which is other than temporary. This may also entail periodically seeking the help of experts to assess the fair value of its investments. **(A further discussion on the fair valuation aspects appears subsequently).**

Current Investments

The broad principles dealing with the measurement of current investments are as under:

- The initial acquisition cost of such investments is determined on the same lines as discussed above for long term investments.
- In subsequent years/periods, the carrying amount for current investments is the *lower of cost and fair value.*
- Valuation of current investments on overall (or global) basis is not considered appropriate. Sometimes, the concern of an enterprise may be with the value of a category of related current investments and not with each individual investment, and accordingly the investments may be carried at the lower of cost and fair value computed category wise (i.e., equity shares, preference shares, convertible debentures, etc.). However, the more prudent and appropriate method is to carry investments individually at the lower of cost and fair value.
- Any reduction to fair value and any reversals of such reductions are included in the profit and loss statement.

In respect of investments for which an active market exists, market value generally provides the best evidence of fair value. However, the challenge arises in respect of investments which are not listed. This may also entail periodically seeking the help of experts to assess the fair value of its investments. ***(A further discussion on the fair valuation aspects appears subsequently).***

The valuation of current investments at lower of cost and fair value provides a **prudent method** of determining the carrying amount of the investment.

After having examined the measurement aspects under Indian GAAP let us proceed to examine the same under Ind AS, as applicable to certain prescribed classes of companies and which are far more complex.

Ind AS

The measurement of shares is dealt with under **Ind AS-109** which deals with Financial Assets read with **Ind AS-32** which deals with the classification of Financial Liabilities between Debt and Equity Instruments from the issuers perspective which as we will examine shortly is also relevant from the holders perspective.

We will now examine the various aspects relevant to measurement of shares as dealt with under Ind AS-109 and 32.

Meaning and Nature of Financial Assets

Ind AS-32 defines a financial asset as any asset that is:

a) Cash

b) An ***equity instrument of another entity***

c) A contractual obligation to receive cash or another financial asset from another

entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity.

As can be seen above, an **equity instrument needs to be evaluated from the perspective of an issuer** and the same is **defined in Ind AS-32** as *any contract that evidences a residual interest in the assets of an entity after deducting all its liabilities.* Accordingly, from the point of view of the holder, an equity instrument is an asset/instrument in which the entity does not have a right to receive a fixed contractual amount of principal or interest. Accordingly, by default any instrument which does not meet the definition of an equity instrument from an issuer's perspective would be regarded as a debt instrument in which there is generally a contractual cash flow involved. *Hence all investments in equity shares as well as convertible preference shares would be regarded as an equity instrument whereas all investments in redeemable preference shares would be regarded as a debt instrument.*

Once we have understood the above difference the next step is to assess the business model under which the various classes of shares can be held by a company.

Business Model Assessment

Assessing the business model for holding financial assets is the anchor on which the entire accounting for financial assets rests. However, before going into the assessment of the business model, it would be relevant to understand the fundamental principle for initial measurement of all types of financial assets, irrespective of the business model for holding the same.

Initial Measurement of Financial Assets

As per Ind AS-109 an entity shall **initially measure** its financial assets at ***its fair value plus or minus any transaction costs that are directly attributable to the acquisition of the financial assets in case of those falling under the FVTPL category (discussed later).*** This represents a paradigm shift from the cost model of measurement adopted under Indian GAAP which we have seen earlier.

The **best evidence of the fair value on initial recognition is normally the transaction price.** However, if the company determines that the fair value based on quoted prices in an active market for identical items or based on observable and unobservable inputs like interest rates, yields, credit spreads etc., is different the same shall be recognised as a day one gain or loss. In the context of shares, this may be relevant for investment in ***redeemable preference shares which have a nil or negligible rate of dividend.***

Classification of Financial Assets

Under Ind AS-109, understanding the business model under which financial assets are held are held is the key criteria for determining their classification and subsequent measurement and accounting. Ind AS-109 requires that all financial assets are required to be **classified under the following three categories for subsequent measurement purposes:**

a) **Amortised Cost**

b) **Fair value through profit or loss (FVTPL)**

c) **Fair value through other comprehensive income (FVTOCI)**

The classification depends upon the following **two criteria and options elected by the entity:**

a) The entity's business model for managing the financial assets, and

b) The **contractual cash flow characteristics** of the financial assets.

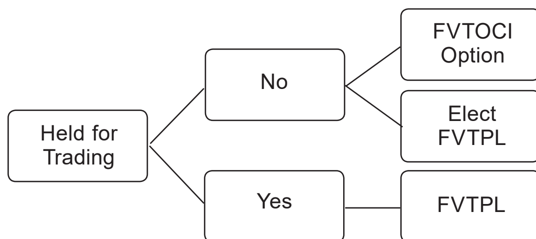
Further, there are **separate classification requirements** for:

a) **Equity Instruments (applicable to equity shares and fully convertible preference shares for the purposes of this article)**

b) **Debt Instruments (applicable to redeemable preference shares for the purposes if this article)**

Equity Instruments

Since equity instruments do not involve the right to contractually receive fixed and determinable cash flows whether through principal and interest, their classification is more ***dependent upon the intention of whether it is "held for trading"*** (discussed later). However, in situations in which the instruments are *not held for trading, the entity needs to exercise an irrevocable choice* as to whether it wants to elect the *FVTOCI option*. A tabulation of the choices available is depicted hereunder.



Accordingly, all equity instruments which are "held for trading" are required to be mandatorily classified as FVTPL, whereas for all other instruments, the entity can make an irrevocable option to classify the same as FVTOCI or **elect the FVTPL option** (discussed later). The following are some of the **key points** which are relevant regarding the **FVTOCI classification of equity instruments**:

a) Classification as FVTOCI is not mandatory though it cannot be used for equity instruments "held for trading".

b) The classification needs to be made on initial recognition and it irrevocable.

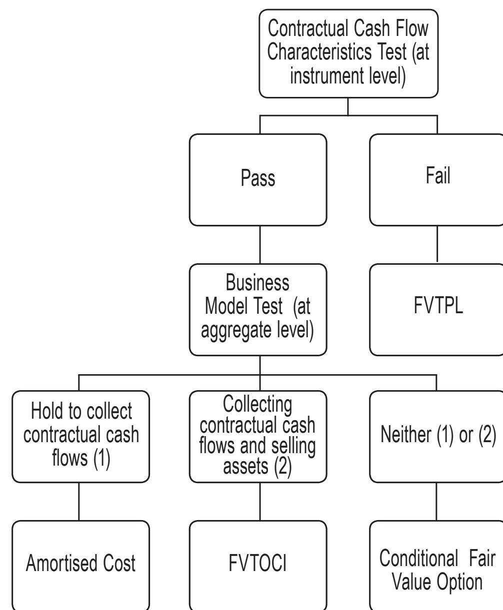
c) The election can be made on an instrument by instrument basis and is not an accounting policy choice.

d) If the entity elects this option then all fair value changes on the particular instrument, excluding dividends are recognised through OCI and no recycling is permitted to Profit and Loss even on disposal, though the cumulative gain or loss at the time of disposal may be transferred within equity to retained earnings.

e) There are no separate impairment requirements.

Debt Instruments

The classification of debt instruments is dependent upon the business model which refers to how an entity manages its financial assets so as to generate cash flows i.e. whether the entity ***will collect the cash flows by holding the financial asset till maturity or sell those assets or both.*** A tabulation of the choices available is depicted hereunder.



The following are some of the key points which are relevant regarding the FVTOCI classification of debt instruments:

a) For debt instruments meeting the above prescribed criteria, FVTOCI classification is ***mandatory, unless FVTPL option is exercised as discussed below.***

b) For such debt instruments, interest income, impairment and foreign exchange changes are recognised in profit and loss whereas all other changes are recognised directly in OCI.

c) On derecognition, cumulative gains and losses previously recognised in OCI are reclassified from equity to profit and loss.

Option to Designate a Financial Assets at FVTPL

Irrespective of the satisfaction of any of the above conditions for amortised cost or FVTOCL designation, Ind AS-109 provides an option to irrevocably designate a financial asset as measured at FVTPL if doing so ***eliminates or significantly reduces a measurement mismatch which is also referred to as an 'accounting mismatch'*** which would otherwise arise if a different basis is followed. Though this is an accounting policy choice, it is not required to be applied consistently for all similar transactions. Ind AS-109, provides the following guiding principles to designate financial assets as measured at FVTPL:

a) When the financial asset is part of a hedging relationship.

b) When the financial assets, financial liabilities or both share a common risk such as interest rate risk that gives rise to offsetting changes as part of the entity's ALM policy.

c) When a group of financial assets are managed and performance is evaluated on a fair value basis such as investment management, venture capital companies or stock broking companies.

Held for Trading

Apart from the option to designate financial assets at FVTPL as discussed above, another important consideration for FVTPL designation is whether the financial assets are "held for trading" for which Ind AS-109 has provided certain guiding principles which are briefly discussed hereunder:

a) The financial assets are acquired 'principally' for the purpose of selling in the near term e.g., stock in trade held by a stock broker.

b) The financial asset is part of a portfolio of financial instruments that are managed together and for which there is evidence of a recent actual pattern of short term profit taking.

c) 'Trading' generally reflects active and frequent buying/selling with the objective of generating a profit from short term fluctuations in the price. However, churning of portfolio for risk management purposes is not necessarily 'trading' activity.

Guiding Principles for Assessing the Business Model

The following are some of the guiding principles laid down in Ind AS-109 which need to be considered whilst assessing and determining the business model for managing financial assets, in the context of debt instruments:

a) Assessing the entity's business model for managing financial assets is a matter of fact and not merely an assertion. It has to be based on relevant and objective evidence including but not limited to how the performance of the business model

and the financial assets held within the same are evaluated by the entity's key management personnel, their risks and how the personnel are compensated.

b) The assessment is based on how groups of financial assets are managed to achieve a particular business objective and is *not an instrument by instrument analysis though at another level it is also not an entity level assessment.*

c) A few exceptions against the stated portfolio objectives may not necessitate a change in the business model e.g. a few sales out of a portfolio which is on the "hold to collect" business model. In such situations what needs to be considered are factors like the frequency, timing and reasons for the sales and expectations of the future sales activity.

d) Business model assessment is done based on scenarios reasonably expected to occur and not on exceptional or extreme situations such as 'worst case scenario' or 'stress case scenario'.

Amortised Cost – Business Model Test

Some of the key features for assessing the business model test of holding on to a financial asset for amortised cost determination are as under:

a) To evaluate the entity's business model to hold financial assets to collect contractual cash flows, the ***frequency, value and*** *timing of* ***sales in prior periods and the reasons for such sales have to be analysed.*** Also, future expectations about such sales is required to be analysed. It is important to bear in mind that higher or lower sales than the previous expectations is not a prior period error.

b) In real time business it is not always practical to hold all the financial assets until their maturity, regardless of the business model. Hence, some amount of selling/buying or so called 'churning of portfolio' is expected and permitted. However, if ***more than infrequent number of sales are made out of a portfolio or those sales are more than insignificant in value,*** then there will be a need to assess and validate how such sales are consistent with the business model whose objective is to collect contractual cash flows.

Amortised Cost – Cash Flow Characteristics Test

Another equally important test or criteria to be met for classification of financial assets as subsequently measured at amortised cost is the characteristics of the cash flows arising from the financial asset. Ind AS-109 provides that for this purpose, **the contractual terms of the financial asset should give rise on specified dates to cash flows that are solely payment of principal and the interest on the principal outstanding (SPPI).**

Ind AS-109 **defines interest,** for the purpose of the above assessment as consideration for the following:

a) the **time value of money.**

b) credit risk associated with the principal amount outstanding during a particular period of time.

c) other basic lending risks (such as **liquidity risk) and costs** (such as administration for holding the financial asset.

d) **profit margin.**

Ind AS-109 **defines principal,** for the purpose of the above assessment as **fair value** of the financial asset at the date of initial recognition. This initial amount may change subsequently if there are repayments of the principal amount.

For the purposes of the above assessment, principal and interest payments should be in the currency in which the financial asset is denominated.

The terms of issue of ***redeemable preference shares in which the company has made investments would need to be closely reviewed to determine their correct classification and corresponding subsequent measurement and consequential accounting treatment.***

Key Implementation and Transition Challenges

The current requirements for classification and accounting for investments by companies were quite simple and hence shifting over to an Ind AS regime is expected to present a fair share of challenges both on initial transition and on-going implementation. Further, though all Ind AS requirements are required to be applied retrospectively on the date of transition, Ind AS-101 provides certain exceptions thereto, one of them being that the entity should assess the business model criteria on the basis of facts and circumstances on the date of transition. Finally, the measurement basis for all financial assets on initial recognition would henceforth be at the fair value for which also Ind AS-101 provides for prospective application on or after the date of transition to Ind As. In spite of the aforesaid exemptions from retrospective application, companies are likely to face certain transition and on-going implementation challenges, which are briefly discussed hereunder:

a) **Treatment of existing investments classified as current:** As per the existing AS-13, all investments that by its nature are readily realisable and are intended to be held for not more than one year from the date on which they were made are regarded as current investments. Under Ind AS, all such investments may not automatically meet the held for trading criteria especially in respect of equity instruments, especially if these are continuing for periods in excess of one year on the date of transition. Accordingly, a fresh evaluation of the purpose, nature and intention of such investments would need to be undertaken to categorise them under the appropriate bucket.

b) **Documentation and business model assessment:** The classification requirements based on the criteria discussed above may not be straight jacketed in all cases and would need to be documented in a fair degree of detail based on the activity level and type of business of the Company. The existing risk management and ALM policies especially in case of smaller and unlisted entities would need to be recalibrated to capture the various scenarios under Ind AS.

c) **Fair value determination:** The initial measurement of all financial assets at fair value would be a game changer. Whilst initially the transaction price would be the fair value in many cases, this would need to be carefully evaluated in the case of transactions with related parties, transactions not on an arm's length basis or transactions under duress since in such cases, the fair value at which other market participants enter into the transactions would need to be considered which would represent a day one gain or loss. Finally, the on-going assessment of the fair value especially in case of financial assets which are not readily tradeable or quoted on an active market would present challenges especially in cases where there are not many observable inputs to determine the fair value, since it could be based on significant judgements which more often than not could be biased. This would make it inherently difficult for comparison between entities and also

involve significant costs and efforts which may not be always commensurate with the benefits.

d) **Judgments:** Finally, the assessment of the business model involves significant judgments and assumptions which need to be constantly evaluated by the key management personnel on several matters like determining the frequency and volume of sales so as to rebut the business model of held to sale, whether interest rates reset is on time value and the other criteria discussed earlier, manner of determining the pricing for financial assets and the inputs involved therein since all of this would ultimately impact the business model assessment and the consequential classification and measurement of financial assets.

Fair Value Measurement

As is apparent from the above discussion, fair value determination is required whether for disclosure or measurement purposes for investment in shares. Whilst for quoted shares, the market prices are ordinarily the best indicator of the fair value, the real challenge lies in determining the fair value for unlisted or unquoted instruments. For this purpose, the guidance laid down under **Ind AS-113 on Fair Value Determination** would prove useful. Whilst a detailed discussion on fair valuation is beyond the scope of this article, the following are some of the underlying principles laid down in **Ind AS-113,** which merit attention, especially in the context of equity instruments.

Fair Value Hierarchy

The purpose of laying down a fair value hierarchy as per Ind AS-113 is to increase consistency and comparability in the fair value measurements and disclosures. The basic premise of applying this hierarchy is to enable an entity to prioritise the observable inputs over those that are unobservable. Further greater disclosures are mandated in respect of unobservable inputs adopted due to their inherent subjectivity.

The Standard establishes a fair value hierarchy that categorises into three levels, as discussed below, the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

Level 1 inputs

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date and provides the most reliable evidence of fair value.

Level 1 inputs will be available for many financial assets and financial liabilities, some of which might be exchanged in multiple active markets (e.g., on different exchanges). Accordingly, the emphasis within Level 1 is on determining both of the following:

a) the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability; and

b) whether the entity can enter into a transaction for the asset or liability at the price in that market at the measurement date.

Level 2 inputs

Level 2 inputs are inputs other than quoted prices included within Level 1 that are ***observable*** *(those inputs that are developed using market data, such as publicly available information about actual events or transactions, and that reflect the assumptions that market participants would use when pricing the asset or liability)* for the asset

or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability.

Level 2 inputs include the following:

a) quoted prices for similar assets or liabilities in active markets.

b) quoted prices for identical or similar assets or liabilities in markets that are not active.

c) inputs other than quoted prices that are observable for the asset or liability, for example:

    i) interest rates and yield curves observable at commonly quoted intervals;

    ii) implied volatilities; and

    iii) credit spreads.

d) market-corroborated inputs.

Adjustments to Level 2 inputs will vary depending on the factors specific to the asset or liability, which include the following:

a) The condition or location of the asset;

b) The extent to which inputs relate to items which are comparable to the asset or liability; and

c) The volume and level of activity in the markets within which the inputs are observed.

An adjustment to a Level 2 input that is significant to the entire measurement might result in a fair value measurement categorised within Level 3 of the fair value hierarchy, if the adjustment uses significant unobservable inputs.

Level 3 inputs

Level 3 inputs are ***unobservable inputs*** *(those inputs for which market data are not available and that are developed using the best information available about the assumptions that market participants would use when pricing the asset or liability)* for the asset or liability. Unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. Accordingly, unobservable inputs shall reflect the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk.

Valuation Techniques

After having understood the broad principles underlying fair valuation, an entity would need to determine the valuation techniques which are appropriate in the circumstances and for which sufficient data is available to measure the fair value, whereby there is maximum use of observable inputs and minimum use of unobservable inputs, keeping in mind the overall objective of the valuation exercise to estimate the price at which an orderly transaction to sell an asset or transfer a liability would take place between market participants under current market conditions.

There are three widely used valuation techniques which are prescribed in Ind AS 113 as under:

- Market approach
- Cost approach
- Income approach

Each of these are briefly analysed hereunder:

The Market Approach

This approach uses prices and other relevant information generated by market transactions involving identical or comparable assets, liabilities or group of assets or liabilities. The valuation techniques consistent with the market

approach often use market multiples derived from a set of comparable assets, liabilities or business, as applicable. Multiples might be in ranges with a different multiple for each comparable. The selection of the appropriate multiple within the range requires judgment, considering qualitative and quantitative factors specific to the measurement. Some of the commonly used market multiples are EV/EBIDTA, revenue or matrix pricing involving comparison with benchmark securities.

The Cost Approach

This approach reflects the amount that would be required currently to replace the service capacity of the asset, which is often referred to as the current replacement cost. From the perspective of a market participant seller, the price that would be received for the asset is based on the cost to a market participant buyer to acquire or construct a substitute asset of comparable utility, adjusted for obsolescence, since a market participant buyer would not pay more for an asset than the amount for which it could replace the service capacity of that asset.

For this purpose, obsolescence encompasses the following:

a) physical deterioration,

b) functional (technological) obsolescence, and

c) economic (external) obsolescence

Obsolescence is much broader than depreciation for financial reporting purposes or tax purposes.

The Income Approach

This approach converts the future amounts comprising of cash flows, income or expenses to a single current (discounted) amount. The fair value measure so arrived at reflects the current market expectations of such future amounts. The following are the commonly used valuation techniques under this approach:

- Present value technique
- Option pricing models
- Multi-period excess earnings method

Whilst a detailed discussion on each of these techniques is beyond the scope of this article, some broad principles underlying the present value technique which is most commonly used is covered hereunder.

Present Value Technique

The present value technique is the most commonly used technique and is the only technique for which guidance is provided in Ind AS-113. This technique links the future estimates or amounts (e.g., cash flows or values) to a present amount using a **discount rate**. A fair value measurement of an asset or a liability using a present value technique captures all the following elements from the perspective of market participants at the measurement date:

a) An estimate of future cash flows for the asset or liability being measured.

b) Expectations about possible variations in the amount and timing of the cash flows representing the uncertainty inherent in the cash flows.

c) The time value of money, represented by the rate on risk-free monetary assets that have maturity dates or durations that coincide with the period covered by the cash flows and pose neither uncertainty in timing nor risk of default to the holder (i.e., a risk-free interest rate).

d) The price for bearing the uncertainty inherent in the cash flows (i.e., a risk premium).

e) Any other factors that market participants would take into account in the circumstances.

Valuation Equity Instruments

The valuation of equity instruments is dependent on the underlying valuation of the company which has issued these instruments. For this purpose the appropriate valuation methodology from amongst the various methods as discussed earlier would need to be considered dependent upon the nature of the business/industry and the purpose of the valuation whether on a going concern or liquidation basis etc.

A question which often arises in case of **unquoted equity shares** on the **basis and frequency** with which the fair value needs to be measured due to lack of credible recent information being available and consequently whether the cost can be considered as the fair value. In this context, **para B 5.2.3 of Ind AS 109** provides that *in limited circumstances, cost may be an appropriate estimate of fair value, especially in case if insufficient more recent information is available to measure fair value, or if there is a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range.* Further, **para B5.2.4 of Ind AS-109 provides for a list of some of the following indicators where cost might not be representative of the fair value.** Further the aforesaid indicators are not exhaustive and any other relevant information about the performance and operations of the investee after the initial recognition should be also factored in.

a) Significant change in the performance of the investee compared with budgets, plans or milestones.

b) Changes in expectation that the investee's technical product milestones will be achieved.

c) Significant change in the market for the investee's equity or its products or potential products.

d) Significant change in the global economy or the economic environment in which the investee operates.

e) Significant change in the performance of comparable entities, or in the valuations implied by the overall market.

Disclosure Aspects

The disclosure requirements laid down in the Standards and as prescribed by the regulators are like a **report card of the financial position of the entity and a communication tool to the various users/stakeholders/regulators** and reflect the actual application and compliance with the requirements of the Standards. Let us now proceed to briefly examine the various disclosures separately under Indian GAAP and Ind AS, respectively.

Indian GAAP

The main disclosures which are prescribed under Indian GAAP as per AS-13 read with Schedule III of the Companies Act, 2013, which are relevant for investments in shares are as under:

- Current and long term investments need to be disclosed separately.
- Quoted and unquoted investments need to be disclosed separately, both in terms of the aggregate amount and for individual investments.
- The market value of quoted investments needs to be disclosed by way of a note in the aggregate. ***It is relevant to note that Indian GAAP nowhere requires disclosure of information about fair value of unquoted investments.***
- Provision for diminution in value, other than temporary in respect of long term investments, individually. ***This would involve assessment of their fair value, amongst other factors.***

- Significant restrictions on the right of ownership, realisability of investments or on the remittance of income and proceeds of disposal.
- Interest and dividend income, showing separately the dividend income from subsidiaries, as well as from long term and current investments.
- Profits and losses on disposal of current and long term investments, separately.

The above disclosures are not as comprehensive or detailed as laid down under Ind AS, as discussed subsequently.

Ind AS

These would need to be separately analysed in respect of financial instruments which are laid down in **Ind AS-107 – Financial Instrument – Disclosures and in respect of Fair Values as per Ind AS-113,** to the extent relevant for shares.

Financial Instrument Disclosures

The disclosure requirements with regard to financial instruments which are laid down in Ind AS-107, to the extent relevant for shares are briefly discussed hereunder.

Balance Sheet Disclosures

Categories of Financial Assets:

- **Financial assets measured at fair value through profit or loss,** showing separately: (i) those designated as such upon initial recognition or subsequently in accordance with Ind AS-109 and (ii) those mandatorily measured at fair value through profit or loss in accordance with Ind AS 109.
- **Financial Assets at amortised cost.**
- **Financial assets measured at fair value through OCI, showing separately** (i) financial assets that are so measured in accordance with Ind AS-109; and (ii) investments in equity instruments designated as such upon initial recognition in accordance with Ind AS-109.

Equity Investments designated at FVTOCI

- The specific investments in equity instruments have been designated to be measured at FVTOCI and the reasons for using this presentation alternative.
- The fair value of each such investment at the end of the reporting period.
- Dividends recognised during the period, showing separately those related to investments derecognised during the reporting period and those related to investments held at the end of the reporting period.
- Any transfers of the cumulative gain or loss within equity during the period including the reason for such transfers.
- In case of derecognition/disposal:
  - a) Reasons for disposal
  - b) Fair value on date of disposal
  - c) Cumulative gain or loss on disposal

Allowance for Credit Losses

- The carrying amount of financial assets measured at FVTOCI is not reduced by a loss allowance and an entity shall not present the loss allowance separately in the balance sheet as a reduction of the carrying amount of the financial asset.
- However, an entity shall disclose the loss allowance in the notes to the financial statements

Profit and Loss Statement Disclosures

- Net gains or losses on financial assets measured at FVTPL showing separately those designated as such upon initial recognition or subsequently, and those that are mandatorily measured at FVTPL
- Net gains or losses on financial assets measured at amortised cost.
- Net gains or losses on investments in equity instruments designated at FVTOCI.
- Net gains or losses on financial assets measured at FVTOCI showing separately the amount of gain or loss recognised in OCI during the period and the amount reclassified upon derecognition from accumulated OCI to profit or loss for the period.
- Total interest revenue and total interest expense (calculated using the effective interest method) for financial assets that are measured at amortised cost or that are measured at FVTOCI (showing these amounts separately).

Apart from the above there are various other specific disclosures dealing with risk assessment, collaterals, etc., for the financial instruments as a whole, which are not specifically discussed herein.

Fair Value Measurements [Ind AS-113]

As discussed earlier, the concept of fair value measurements is one of the important ingredients of Ind AS accounting and consequently all entities are required to give certain disclosures when assets and liabilities, especially financial instruments are recognised, even if they are not measured at fair value for the purposes of financial statements. Further, the disclosures are mainly aimed at measurements which use level 3 unobservable inputs which are subjective and judgmental. Accordingly, the disclosures, as relevant for shares can be broadly categorised as under:

- The valuation techniques, inputs and assumptions used in measuring fair value.
- The impact of level 3 fair value measurements on the profit and loss account or other comprehensive income.
- Reasons for non-recurring fair value measurements.
- The fair value hierarchy adopted.
- The reasons for transfer between the hierarchical levels for recurring fair value measurements.
- The valuation techniques adopted, including any changes therein, for both recurring and non-recurring fair value measurements.
- Quantitative information about significant unobservable inputs for recurring level 3 fair value measurements.
- The amount of total gains and losses recognised in profit and loss and OCI, together with line items in which these are recognised, for recurring fair value measurements categorised within level 3 of the fair value hierarchy.
- Sensitivity analysis, both narrative and with quantitative disclosures about the significant unobservable inputs.

Conclusion

The above evaluation is just the tip of the ice-berg on a subject for which there may not always be straight jacketed answers. However, the business model assessment is here to stay and it would impact the way the investments in shares are classified and consequently measured and also impact the auditors and prove to be a *bonanza for specialists to develop fair values, who could laugh all the way to the bank!*

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SS-IX-57

CA Bhavesh Vora

Measurement, Disclosure & Auditing of Derivatives (Listed & Unlisted)

I. INTRODUCTION

India as a country conceptualised the knowledge of derivatives as early as the late nineteenth century when the Bombay Cotton Trade Association introduced the use of forward contracts. At that point in time, risk-averse traders wanted to hedge themselves against the volatility in prices, as a result of which forward trading in a number of other commodities increased over the next few decades. Moving forward, in the year 1952 the Government put a ban on cash settlement and options trading, and the commodities derivatives found its place in the informal segment of the market until the ban was lifted in the year 2000. The Securities Contract Regulation Act, 1956, when introduced, banned all kinds of derivatives trading in equities and it was only in 1999 that there were committees set up to amend this Act.

In the post liberalisation era of India, the increase in market risk and volatility led to the growing demand for an 'Option' like financial derivatives. All factors put together persuaded both BSE and NSE to commence trading in equity derivatives in the year 2000.

Presently, The Bombay Stock Exchange Ltd. (BSE) and The National Stock Exchange of India Ltd. (NSE), primarily facilitate derivatives trading in securities and currencies, whereas The Multi Commodity Exchange of India Ltd. (MCX) and National Commodity & Derivatives Exchange Ltd. (NCDEX) facilitate the same for commodities.

The total turnover of stock futures and options traded on the NSE witnessed an increase by approximately twenty-one times from the year 2008-09 to the year 2018-19. Moreover, the year 2018-19 witnessed a growth of 44% in the turnover from these stock futures and options contracts as compared to the immediate previous year.

Currency derivatives turnover on NSE has seen tremendous growth since the time it was first introduced, fairly representing the future outlook of the Indian derivatives market.

The increasing participation of derivatives in the Indian markets paved the need for recognition, measurement and disclosure of derivatives at

appropriate values to indicate the risk that they expose the entity to.

With introduction of Ind AS, derivatives, falling under Financial Instruments are governed by the principles of Ind AS 109 Financial Instruments, Ind AS 32: Financial Instruments: Presentation and Ind AS 107: Financial Instruments: Disclosures. Fair value measurements and related disclosures are prescribed by Ind AS 113.

II. DEFINING DERIVATIVES

Ind AS 109 defines derivatives as "a financial instrument or other contract within the scope of this Standard with all three of the following characteristics:

a. its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying');

b. it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and

c. it is settled at a future date."

Therefore, derivatives is any financial instrument, which derives its value, in response to a change in underlying, which requires no initial investment, and will be settled on a future date.

Most derivatives contracts are used either for hedging purposes (to change an existing risk position) or trading purposes (to take a risk position to benefit from long term investment results or from short term market movements). A derivative usually has a notional amount, which is an amount of currency, a number of shares, a number of units of weight or volume or other units specified in the contract. However, a holder or writer is not required to invest or receive the notional amount at the inception of the contract. He only needs to invest the applicable margins to enter into and continue with such a contract.

Based on the purpose of the derivatives, the accounting treatment for the derivatives is enumerated by the aforementioned standards.

III. MEASUREMENT OF DERIVATIVES

Measurement of financial instruments seems to be a complex task, more so under the Ind AS framework, with the increased emphasis on fair value measurements.

Ind AS 109 prescribes that a Financial Asset shall be classified as subsequently measured at mortised cost, fair value through other comprehensive income (OCI) or fair value through profit or loss on the basis of:

(a) The entity's business model for managing the financial assets and

(b) The contractual cash flow characteristics of the financial asset.

For a financial asset to be measured at amortised cost or at fair value through OCI, its contractual terms should give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. It must also be held within a business model whose objective to hold financial assets is either to collect contractual cash flows or to both sell the assets and collect contractual cash flows.

The definition of held for trading as given in the standard is "a financial asset or financial liability that: (a) is acquired or incurred principally for the purpose of selling or repurchasing it in the near term; (b) on initial recognition is part of a portfolio of identified financial instruments that are managed together

and for which there is evidence of a recent actual pattern of short-term profit-taking; or (c) is a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument)". Therefore it explicitly includes derivatives.

Financial liabilities may be recognised at amortized cost or at fair value through profit and loss. Derivatives in the nature of financial liabilities are explicitly said to be measured at fair value through profit and loss.

Therefore, all derivatives whether assets or liabilities, except for those which are hedging instruments, will be measured at their fair value through profit and loss.

Initial Measurement

The best fair value at initial recognition is likely to be the transaction price, i.e., the consideration given or received for the instrument. However, if part of the consideration is given or received is for something other than the financial instrument, an entity shall measure the fair value of the financial instrument.

Since derivatives are classified as financial asset or financial liability at fair value through profit or loss, they are initially measured at fair value without making any adjustment for any transaction costs.

Subsequent Measurement

Subsequently derivatives which are assets or liabilities shall be measured at their fair values.

Ind AS 113 prescribes methods for obtaining the fair value of assets and liabilities. Since valuation is a subjective process, involving a large amount of assumptions, estimations and extrapolations, it is important that certain specific standards and methodologies be followed while measuring derivatives to ensure that the same are comparable across periods and entities. These should remain constant in the absence of an appropriate justification for a change in the same. Entities must disclose the valuation methods to enable users to understand the subjectivity involved in the same.

Measurement of Listed Derivatives

Listed derivatives are quoted on an exchange and price information regarding the same is likely to be easily available from the exchange. When such derivatives are regularly traded, the price available on the exchange will represent actual and regularly occurring market transactions on an arm's length basis. The fair value will be determined based on the value it can obtain in its principal market and in the absence of the same from the most advantageous active market that the entity has access to. However, even in these cases it is important to ensure that the management uses appropriate market quotes. It is necessary to ensure that these quotes are not 'out-of-date' or stale and that they are at a reasonable comparable volume. In these cases, evidence for assumptions are more easily available.

Measurement of Unlisted Derivatives

Unlisted derivatives too may have readily available prices in an active deal market or broker market or from certain institutions that can be used as inputs for valuing these derivatives. For example, in the case of interest rate forwards there may be quoted rates available from banks. In such a scenario, the derivatives will be valued in a manner similar to listed derivatives that have active market. In case of derivatives for which this information is not available, other valuation techniques may have to be used. These techniques include using recent arm's length transactions between knowledgeable willing parties, if available and these techniques include using the fair value of the arm's length transaction in some other instrument which is substantially the same, using discounted cash flow analysis, and option pricing models. Pricing data can be obtained from other sources such as brokers or consensus pricing services as well.

Derivatives used as Hedge

Derivatives can be used in risk management to hedge position, protecting against the risk of an adverse movement of an asset. An entity may want to hedge itself against a number of risks such as interest rates fluctuations, foreign currency movements, variations is the prices of securities, variation in market prices of various commodities and similar movements. In such cases hedges are required for entities to be able to set a maximum limit on the amount of loss they will incur from some transaction or to guarantee a minimum profit that they will obtain from the transaction.

A hedging relationship qualifies for hedge accounting where

i. The hedging relationship consists of only eligible hedging instruments and eligible hedged items.

ii. There is a formal designation of the hedging relationship

iii. The hedging instruments meet the below hedge effectiveness requirements

   a) there is an economic relationship between the hedged item and the hedging instrument

   b) the effect of credit risk does not dominate the value change

   c) the hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the entity actually hedges and the quantity of the hedging instrument that the entity actually uses to hedge that quantity of hedged item.

The major categories of hedges are fair value hedges and cash flow hedges. Another type of hedge is the hedge of a net investment in a foreign operation. A fair value hedge is a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, which is attributable to a particular risk. A cash flow hedge is for variability in cash flows.

In a fair value hedge, if the above conditions are met, the gain or loss on the hedging instrument shall be recognized in the profit or loss, except in the cases where the hedging instrument hedges an equity instrument for which the entity has elected to present changes in other comprehensive income.

For a cash flow hedge, a separate component of OCI shall be designated which will be called the cash flow hedge reserve. This reserve is adjusted to the lower of the cumulative gain or loss on the hedging instrument and the cumulative gain or loss in the hedged item.

The portion of gain or loss that is determined to be an effective hedge (the part that is offset by changes in the cash flow hedge reserve) shall be recognized in the OCI, whereas the remaining gain or loss shall be recognized in the profit and loss.

The amount that has accumulated in this cash flow hedge reserve will be accounted for as follows:

i. If the hedged transaction results in the recognition of a non-financial asset or non-financial liability the amount will be transferred to the carrying amount of the asset or liability.

ii. In other cases the amount should be transferred to the profit and loss, as a reclassification adjustment, during the period where the hedged cash flows affect the profit and loss.

iii. However if it is expected that the all or a portion of the amount will not be recovered then it shall be immediately reclassified to profit and loss as a reclassification adjustment.

A hedge in a net foreign investment will be accounted for similarly to a cash flow hedge.

Hedge accounting will be discontinued when the hedging relationship fails to meet the hedging criteria. This includes instances where the instrument is sold or terminated, but not replacement or rollover of the hedging instrument.

IV. DISCLOSURE OF DERIVATIVES

When it comes to derivatives, disclosure requirements go deep into the nature of risks, the nature of inputs used to value them, the other possible inputs that could have been used and other related information. This is because the nature of the instrument is such that it is affected by a large number of variables which may not be easily observable and a lot of additional information is required to understand them well.

Major disclosures that would be applicable to derivatives are as under:

General Disclosures

All derivatives shall be classified and disclosed as either of the following:

Financial assets/financial liabilities at fair value through profit or loss, showing separately

a. those designated as such upon initial recognition and

b. those mandated as such Ind AS 109;

For any liabilities designated as financial liability through profit and loss the entity shall disclose the amount of change attributable to change in credit risk of the liability either as change that is not attributable to a change in credit risk of the liability or by using any other method that would more accurately depict the same. These disclosures should include the methods used for the same.

The entity shall also disclose the maximum exposure to credit risk and the extent to which the same is mitigated by credit derivatives or other similar instruments.

If the requirements to disclose assets and liabilities in the balance sheet as offsetting are met, the entity shall disclose information to enable users to evaluate the effect or potential effects of the netting off.

Derecognition: For financial assets or financial liabilities that have been transferred and Derecognised, but in which the entity has a continuing involvement, the entity shall disclose the carrying amount of the assets and liabilities, their fair value that represents the entity's continuing involvement, the amount that represents the entity's maximum exposure to loss, the undiscounted cash flows that may be required to repurchase the same with a maturity analysis, and any qualitative information that may be required to understand the above.

Collateral : The entity shall disclose any financial assets that it has pledged as collateral along with the terms and conditions of the pledge. It shall also disclose the details of any collateral it holds that it is permitted to sell or repledge even in the absence of a default by owner.

Embedded derivatives : If the entity has issued an instrument that has both, liability and equity and multiple embedded derivatives, the existence of all such features shall be disclosed.

Net Gain or Loss- The entity shall disclose any net gains or losses on each individual category of financial assets and liabilities. The gains or losses on derivatives will fall under net gains or losses on financial assets or financial liabilities at fair value through profit and loss.

Basis of measurement and Accounting Policy : The measurement basis and other accounting policies that are relevant to understanding financial statements must be disclosed.

Disclosures for hedge accounting

Disclosures pertaining to hedge accounting shall provide detailed information about the following:

- The entity's risk management strategy.
- Effect of hedge accounting on the amount, timing and uncertainty of cash flows.
- The effect of the same on balance sheet, profit and loss, and statements of equity.

For fair value hedges the entity shall disclose in a tabular format:

Related to hedged item

i. Carrying amount of hedged item

ii. Accumulated amount of fair value adjustments included in the above.

iii. The line item in balance sheet where the hedge is included.

iv. The change in value of the hedged item used as basis to recognize the hedge ineffectiveness.

v. Accumulated amounts remaining in balance sheet.

Related to hedge

i. Hedge ineffectiveness

ii. Line item where the ineffectiveness is recognized

For cash flow hedges and hedges of a net investment in a foreign operation the entity shall disclose in a tabular format:

Related to hedged item

i. The change in value of the hedged item used as basis to recognize the hedge ineffectiveness.

ii. The balances remaining in the cash flow reserve and the foreign currency translation reserve.

iii. The balances remaining from hedging relationships to which hedge accounting is no longer applied.

Related to hedge

i. Hedging gains or losses recognized in the OCI.

ii. Hedge ineffectiveness recognized in profit and loss and the line item it which it is recognized.

iii. The amount reclassified from the cash flow reserve or the foreign currency translation reserve.

iv. The line item that includes the reclassification.

v. for hedges of net positions, the hedging gains or losses recognised in a separate line item in the statement of profit and loss.

Fair Value Measurement and Hierarchy

For the purposes of determining fair value, the available inputs are to be divided into three levels.

1. Level 1 inputs- Quoted prices in active market
2. Level 2 inputs- Inputs other than quoted prices that are observable
3. Level 3 inputs- Inputs are not based on observable market data

Based on the above levels the entity shall disclose for all instruments the level in the fair value hierarchy to which the fair value measurements belong, and any transfers between level 1 and level 2 hierarchy

For fair value measurements with level 3 hierarchy the entity must prepare a reconciliation showing:

a. Total gains or losses recognised in profit and loss.

b. Total gains or losses recognised in other comprehensive income

c. Purchases sales issues and settlements

d. Transfers in and out of level 3

Fair Value Measurement Hierarchy disclosures could be as under:

Financial Assets	*31/03/2019*			*31/03/2018*		
	Level 1	*Level 2*	*Level 3*	*Level 1*	*Level 2*	*Level 3*
Financial Assets						
Quoted derivatives	xx			xx		
Investment in unquoted equity shares			xx			xx
Financial Liabilities						
Derivatives		xx			xx	

Level 1 hierarchy includes financial instruments values using quoted market price. Listed securities have been included here.

Level 2 hierarchy includes instruments without quoted value in active market. This includes over the counter derivatives. These have been reported at discounted value and thus recorded at level 2.

Level 3 includes investments in unquoted equity shares that are not based on any observable market input.

Nature and Extent of Risks in Financial Statements

The entity should make clear disclosures of the nature of risk and the exposure to risk that the derivatives experience. These include:

Qualitative Disclosure

For each type of risk an entity shall disclose the below and any changes that occur in the same.

a. The exposure to risks and how they arise

b. The objectives, policies and processes for managing risks

Quantitative disclosures

a. Summary quantitative data and exposure to risk

b. Disclosures related to credit risk

c. Concentration of risk if the same is not apparent

Credit Risk

For every financial instrument the entity shall disclose the amount that best represents its maximum credit risk, except if the same is represented by the carrying value itself. And a description of collateral held as security

Liquidity Risk

The entity shall disclose a maturity analysis for those derivative financial liabilities for which contractual maturities are essential for an understanding of the timing of cash flows and a description of how it manages the liquidity risk inherent in the same.

Market Risk

The entity shall disclose one of the below:

a. a sensitivity analysis for each type of market risk, and methods and

assumptions used to prepare the same, and any changes in these methods or assumptions compared to the previous year.

b. a sensitivity analysis such as value at risk that reflects the interdependencies between risk variables including the method used in preparing it and the objectives and limitations of the said method.

If the sensitivity analysis is unrepresentative of the risk inherent to the financial instrument, the entity shall disclose the fact.

A disclosure made for the above purpose of understanding the nature and extent of risks could be as follows:

(i) Market Risk

The company may have foreign currency exchange risk on procurement of capital equipment. The company manages this risk using derivatives when required.

(a) Exposure to foreign currency risk

Currency	*31/03/2019*	*31/03/2018*
USD	xx	xx

(b) Impact of increase/decrease in exchange rates:

Currency	*Change in Rate/Price*	*31/03/2019*	*31/03/2018*
USD	xx	xx	xx

(ii) Liquidity Risk

The company determines its liquidity requirements in short, medium, and long term and manages its liquidity risk accordingly.

Maturity Analysis

Particulars	*Less than 1 year*	*1 year to 2 years*	*2 years to 5 years*	*More than 5 years*	*Total*
Contractual maturities of financial liabilities as at 31/03/2019					
Fx Forwards	xx	xx	xx	xx	xx
Contractual maturities of financial liabilities as at 31/03/2018					
Fx Forwards	xx	xx	xx	xx	xx

(iii) Credit risk

Company has diversified portfolio of investments with various counter parties with secure credit rating. Credit limits and exposures are actively monitored by the company.

V. AUDITING OF DERIVATIVES

Complex financial instruments deal with a large amount of variable cash flows which are based on multiple market conditions. Derivatives therefore require special attention and skill while they are being audited.

A major risk associated with derivatives is that the management and those charged with governance may themselves not fully understand the risk of using these instruments, or have the expertise to value them correctly, and therefore they may not be able to implement sufficient controls over the same.

Institute of Chartered Accountants of India though its various pronouncements that have spelt out the various risk, controls and procedures that must be incorporated in the conduct of the audit, to help increase its effectiveness.

Internal Control

The auditor must examine and understand the internal control system of the entity to determine the impact of the same on the scope of audit and on audit procedures.

An effective internal control system over complex financial statements should include the following:

a) Presence of Control environment:

b) Control Activities that should be carried out by the entity:

c) Monitoring of controls

d) Understanding the Risk

Audit Procedures

The auditor should keep in mind the following aspects and procedures while carrying out the audit of derivatives:

1. Understanding the instrument
2. Using the work of an expert
3. Understanding the usage of Financial Instruments in the entity
4. Dual purpose tests
5. External Confirmations/confirmations with documents Understanding the Managements Method of Valuation
6. Sources of Inputs to a Valuation method
7. Consistency across audit periods
8. Audit of Disclosures
9. Using the work of Internal Auditors

Further, the Independent Auditor's Report requires reporting on provisioning for material foreseeable losses, if any on long-term contracts including derivative contracts as required under applicable laws and accounting standards.

VI. CONCLUSION

The emergence and quick growth of complex financial instruments have made it necessary to warrant them special attention while preparing and auditing Financial Statements. The above evaluation is just a summary explanation and requires far detailed examination. Their complexity makes them susceptible to misstatements, which could arise both from error and from fraudulent intent and makes it essential to have appropriate disclosures so that users of the financial statements can appropriately understand them and the risks attached to them. With more derivative products securing advance and being used by companies, it is imperative that thorough understanding is obtained before entering into such transactions and giving opinion of the same.

Sources:

1. Futures and options derivatives: https://www.nseindia.com/products/content/derivatives/equities/historical_fo_bussinessgrowth.htm
2. Currency Derivatives: https://www.nseindia.com/products/content/derivatives/currency/cd_historical_businessGrowth.htm
3. RBI Report of the Working Group on Reporting of OTC Interest Rate and Forex Derivatives- 25 May 2011:

   https://www.rbi.org.in/scripts/PublicationReportDetails.aspx?ID=633#CH1
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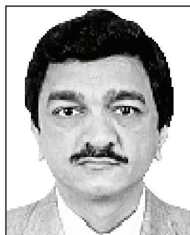

B. V. Jhaveri, *Advocate*

DIRECT TAXES

Supreme Court

1. The High Court upheld Tribunal's order deleting penalty under Section 271(1)(c) on the ground that addition on account of alleged stock was not as a result of purchases made outside books of account, but was only on account of wrong entries in the books of account - SLP dismissed

Principal Commissioner of Income-tax, Bengaluru vs. Deccan Mining Syndicate (P.) Ltd. [2019] 105 taxmann.com 138 (SC)]

For A.Ys. 2007-08 to 2010-11 the first reason for which penalty in question was imposed by the Assessing Authority in the present case was on account of the excessive deduction claimed under Section 10B of the Act which was set aside by the learned Tribunal, following the decision of this Court in the case of *CIT vs. Tata Elxsi Ltd. [2012] 17 taxmann.com 100/204 Taxman 321/349 ITR 98 (Kar).* Another ground on which the penalty was imposed by the Assessing Authority was the additions made in the income on account of alleged excess stock, holding which too was set aside by the learned Tribunal *vide* Paragraph 17 of the impugned order quoted above holding that the said alleged excess stock was not as a result of purchases made outside the books of accounts, but was only on account of wrong entries in the books of account and in any case the higher stock-in-trade declared as closing stock in a particular year would be taken as opening stock at the beginning of the next year and therefore the tax effect of such alleged excess stock is 'Nil' and thus it being a tax neutral entry, the learned Tribunal found that there was no concealment on the part of the assessee, attracting penalty under Section 271[1][c] of the Act.

The Karnataka High Court dismissing the appeal of the Revenue held that since the Tribunal has reiterated the findings of facts that both the additions made to the income of the Assessee having been set aside following the decision of the High Court in the case of *Tata Elxsi Ltd., [supra]* as far as issue of Section 10B is concerned and on the issue of excess stock being tax neutral, such cogent and reasonable findings of facts returned by the learned Tribunal and consequentially setting aside the penalty under Section 271[1][c] of the Act, does not give rise to any substantial question of law requiring the consideration by this Court under Section 260-A of the Act.

The Supreme Court did not see any reason to interfere in the matter and accordingly the SLP of the Revenue was dismissed.

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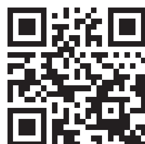

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Paras S. Savla, Jitendra Singh, Nishit Gandhi, *Advocates*

DIRECT TAXES

High Court

1. Exemptions to Educational Institutions – Section 10(23C)(iiiab) – Grants received from Government – meaning of the word 'substantially financed' discussed – Grants is more that 50 % during the year and hence exemption cannot be denied. (AY 2004-05, 2006-07 & 2007-08)

ADIT (E) /s. Tata Institute of Social Sciences – ITXA Nos. 1179 of 2013 and 1321 & 1322 of 2016, Bombay High Court, order dt. 26 March, 2019

Assessee, registered as a Trust under Section 12-A of the Act, claimed exemption from tax under Section 10(23C) (iiiab) of the Act. The Assessing officer (AO) observed that the amount of Government grant of ₹ 12.79 Crores as received was less than 75% of the total expenditure of ₹ 16.87 Crores. The AO while accepting the claim that the Assessee was existing solely for educational purposes denied the benefit of Section 10(23C)(iiiab) of the Act on the grounds of not being substantially financed by the Government. The measure of 75% was arrived at by taking aid of/referring to Section 14 of the Controller Auditor General's (Duties, Powers and Conditions of Service) Act, 1971 ("CAG Act") and after so holding the AO denied the exemption. This assessment order was challenged in appeal by the Assessee before the Commissioner of Income Tax (Appeals) [CIT(A)]. The CIT(A) allowed the appeal of the Assessee holding that the provisions of CAG Act will not be applicable to the Act in the absence of any reference to it. The CIT(A) further relied on the Judgement of the Hon'ble Karnataka High Court in the case of CIT v. Indian Institute of Management [2010] 8 taxmann.com 239/[2011] 196 Taxman 276 which in turn relied upon *CIT v. National Education Society (IT Appeal No.808 of 2009)* wherein it was held that, a grant of approximately 37% from the Government out of the total receipts was held to satisfy the meaning of the words 'substantially financed' by the Government. Against the said order the Revenue filed an appeal before the Tribunal which was dismissed by the Tribunal. Against the said order the Revenue filed an appeal before the Hon'ble High Court. The High Court had to decide on whether the assessee was not

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wholly or substantially financed by the Govt. in view of explanation to sub section (1) of section 14 of the Comptroller and Auditor General (Duties, Powers and Conditions of Services) Act, 1971 as the total Govt. grant during the year is less than 75% of the total expenditure of the assessee, more so when the provision of the Income Tax Act is silent on the issue. The High Court held that, there is no basis for invoking the meaning of 'substantially financed' found in the CAG Act for the purposes of Section 10(23C)(iiiab) of the Act, Firstly, the provisions of the CAG Act are neither incorporated nor cited in section 10(23C)(iiiab) or in any other provisions of the Act; secondly the scope and the purpose of the two Acts i.e. CAG Act and the Act are entirely different. The Court held that CAG Act had no application to funds received by an Institution from the Government through the University Grant Commission since the words 'substantially financed' in Section 10(23C)(iiiab) of the Act are used in the context of Government grants of finance to the educational Institutions and therefore, the scope and the ambit of the two Acts i.e. CAG Act and the Income Tax Act are completely different and cannot even be remotely said to be in pari materia. The Hon'ble High Court relied on the judgement of the Hon'ble the Supreme Court in the case of *Msco (P.) Ltd. v. Union of India 1984 taxmann.com 491* which held that it would be hazardous to interpret a word in accordance with its definition in another statute, when it is not dealing with a cognate subject and it will lead to a new terror in legal construction. The Hon'ble Court further observed that one may look into the meaning given to particular words in a different statute provided the other Act is in pari materia with the statute being interpreted i.e. when they relate to the same person or thing or class of persons or things or have the same object and operate in the same field. Another aspect dealt with in arriving at the conclusion against the Department was that after 2014, the measure of the words 'substantially financed' has to be found only by determining the grants received from the Government as a percentage of total receipts received by an institution and not with expenditure. W.e.f. 1-4-2015 an Explanation had been introduced in the said section so as to define the expression "substantially financed by the Government". As stated in Explanatory Notes to the provisions of Finance (No.2) Act, 2014, absence of definition of the phrase 'substantially financed by the Government' had led to litigation and varying decision of various judicial fora, leading to uncertainty in this regard and hence the amendment. Therefore the Explanation to Section 10(23C)(iiiab) of the Act was to clarify the position/meaning of the words 'substantially financed' by the Government' to remove the vagueness attributable to the meaning of the said words by the addition of the Explanation to Section 10(23C)(iiiab) of the Act read with Rule 2BBB of the Rules, which state that grant should be in excess of the prescribed receipts in context of total receipts (including voluntary donations). Rule 2BBB of the Rules provides that the Government grant should be at 50% of the total receipts. The High Court relying on the Judgements of the Hon'ble Supreme Court in the case of State of Bihar v. S.K. Roy AIR 1966 SC 1995 and in the case of *Thiru Manickain & Co. vs. State of Tamil Nadu AIR 1977 SC 518* concurred with the view that an amendment to the Act which is not retrospective may yet be used as an exposition of the Parliamentary intent as contained in the Section even before its amendment. Thus, without holding that the

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Explanation, inserted w.e.f. 1st April, 2015, is retrospective the court used the same as an aid in construing the ambiguous provision to dismiss Revenue's appeal. The Court held that Assessee fulfilled the criteria of being substantially financed by Government and thus granted the exemption u/s 10(23C).

2. Capital gains – Cost of acquisition and cost of improvement – Mortgage created on the property after purchasing the property cannot be treated as cost of acquisition or cost of improvement – Principle of diversion of income by overriding title does not apply (AY 1995-1996)

Smt. D. Zeenath vs. ITO – (2019) 105 taxmann.com 298 (Madras)

The assessee Smt. D.Zeenath along with two other co-owners, namely, Smt. S.A. Kathija Nachial and Smt. Zubaida had originally purchased land measuring 43,596 sq.ft. at Saram Village, Pondicherry, by two sale deeds dated 11.07.1980 and 4-2-1981 for a total consideration of ₹ 2,01,000/-. The property had been offered as collateral security in a loan obtained by M/s. M.O. Hassan Kuthoos Maricar Pvt. Ltd., from State Bank of India, Pondicherry, to an extent of ₹ 3.75 Crores, and the assessee and the other two co-owners stood as guarantors, for the said loan. Mortgage was by deposit of title deeds. No registered mortgage deed was executed. Since the loan was not repaid, the assessee and the other two co-owners consented for sale of the property by Bank to realize its dues. This was purchased by M/s. Royal Park, Tiruchirapalli, for a total consideration of ₹ 1,96,18,200/-. The sale was effected during the Assessment Year 1995-1996. The total sale consideration was paid to the Bank by the purchaser M/s.Royal Park, Tiruchirapalli. The assessee did not file her Returns under section 139(1) of the Act, till 05.03.1998. She filed it belatedly on 06.03.1998 declaring a total income of ₹ 55,26,120/-. The assessment was re-opened under Section 147 of the Act and notice was issued under Section 148 on 24-3-1998. The assessee in her reply initially sought to treat the return filed on 6-3-1998 as the one filed in response to the notice under Section 148 of the Act. She then filed a revised return admitting an income of ₹ 74,580/-. She claimed that since the entire sale consideration had been paid towards the loan account of M/s.M.O.Hassan Kuthoos Maricar Pvt. Ltd to the State Bank of India, Pondicherry, she had not earned any capital gains on the sale of the property. The Assessing Officer rejected the said contention. The assessment order was challenged in appeal before the CIT(A) and thereafter the Tribunal which was upheld by both the authorities. The Assessee further filed an appeal before the Hon'ble High Court. High court was posed with the question as to whether there was a diversion of the sale proceeds towards redeeming the interest of the mortgagor and therefore the amount so diverted was not liable to capital gains tax. This question was raised on the fact that no part of sale consideration was received by the appellant and same was directly paid to the Bank by the purchaser in discharge of the mortgage amount. The High Court held that if the mortgage was created by the assessee himself, then it was not a case where the property had been mortgaged by the previous owner and the assessee had acquired only the mortgagor's interest in the property mortgaged and by clearing the same, he had acquired the interest of the mortgagee in the said property. In fact the mortgage deed was never registered and

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State Bank of India, Pondicherry did not have a right to bring the property to sale. The assessee in the present case, continued to have title over the property along with her co-owners. They brought the property to sale through Bank and as such there was no diversion of sale proceeds by virtue of overriding title, but on the contrary, there was only a mere application by the owners themselves of the profits realized on the sale of land towards the discharge of loan obligations of the firm. It was further held that the assessee cannot claim any part of such application as cost of acquisition for the purpose of computing capital gains as per the provisions of Section 48 of the Act. The Hon'ble High Court, relying on *V.S.M.R. Jagadishchandran vs. CIT [1997] 227 ITR 240 (SC)* dismissed the appeal.

3. Online filing of return - Amendment in section 10AA to deny carry forward of losses from ineligible units w.e.f. AY 2018-2019 – E-filing software cannot determine whether an Assessee can carry forward losses of ineligible unit – Directions issued to accept manual return (AY 2017 – 2018)

Cosmo Films Ltd. vs. CBDT – WP(C) 3598/2019 & CM Appl. No.16512/2019, Delhi High Court, order dt.14-05-2019.

The Assessee company was engaged in the business of manufacturing Bi-axially Oriented Polypropylene Films ('BOPP') and also exported BOPP films. The Assessee company had manufacturing units set up both in the Domestic Tariff Area ('DTA') as well as Special Economic Zone ('SEZ'). It qualified as an 'entrepreneur' as defined in Section 2(j) of the Special Economic Zones Act, 2005 and had been allowed deduction under Section 10AA of the Income Tax Act, 1961 ('Act') since Assessment Year (AY) 2014-15. In its return for AY 2017-18, filed on 29th November 2017, the Company reported an income as regards its SEZ Unit, under the head 'Profit and Gains of Business and Profession' (PGBP) to the tune of ₹ 52,55,59,560/-. This SEZ Unit (otherwise referred to as 'the eligible unit') was eligible to claim deduction under Section 10AA. Following the decision of the Supreme Court of India in *CIT v. Yokogawa India Ltd. (2017) 391 ITR 274 (SC)* the Assessee first calculated the PGBP of the eligible unit separately by claiming the deduction under Section 10AA in Form ITR-6. The losses of ₹ 33,80,37,785/- arising from ineligible unit i.e. the unit set up in the DTA, were not taken into account while calculating the PGBP of the eligible unit. Audit Report was also enclosed, in the prescribed format under Section 10A(5) of the Act read with Rule 16D of the Income Tax Rules, 1962. However while filing the return online, in the reflection in the computation of total income, the claim of deduction was not accepted. The software of the Department did not permit the Assessee's claim under Section 10AA without setting off the loss of the ineligible unit. As a result the entire loss of the ineligible unit got set off against the PGBP of the eligible unit. The net losses of the ineligible unit which were to be carried forward was thus brought down to 'Nil'. The Assessee filed an application before the jurisdictional Assessing Officer ('AO') on 3rd August, 2018 pointing out to the above discrepancy in the online filing of Form ITR-6. Hard copy of the income tax return was enclosed with the letter and the Assessee requested that it be acted upon so that the carry forward of the losses of the ineligible unit would not be denied. This was followed by a representation on 15th November, 2018

to the Central Board of Direct Taxes ('CBDT') invoking its jurisdiction under Section 119(2) of the Act. The Assessee company pointed out that it is facing genuine hardship due to being unable to carry forward the losses of the ineligible unit. This was followed by reminders on 21st January, 13th February, and 25th March, 2019, but in vain. Hence it filed a writ petition before Delhi High Court for direction to CBDT and the Assessing officer to accept its return of income for Assessment Year (AY) 2017-18 manually since it has not been permitted to carry forward the business losses because of a programming difficulty which precluded the Assessee company from claiming it while filing its return online in Form ITR-6. In reply, the department filed a counter affidavit wherein it stated that amendment to section 10AA, with effect from 1st April, 2018 was to overcome the decision of the Supreme Court in Yokogawa India Ltd. (supra). The system was changed in lines with the amendment. The Court held that it was abundantly clear that the amendment in Section 10AA takes effect only from 1st April, 2018 and would apply only from AY 2018-19, it is clear that for all the AYs prior to 2018-2019, the law explained by the Supreme Court in *Yokogawa India Ltd. (supra)* would apply. This is not even disputed by the Revenue. Thus it becomes incumbent on the Respondents to correct the E-filing software to enable the implementation of the decision in *CIT vs. Yokogawa India Ltd. (supra)*. In other words, it will not be open to the Respondents to contend that the E-filing software will determine whether an Assessee can carry forward losses of ineligible unit. The software would have to be changed to comply with the legal requirement and not the other way round. The Court observed that the issues arising from transiting to an online system have been dealt with earlier by the Courts. In each such instance, when faced with the situation of a software glitch that prevents an Assessee from either filing a return or claiming a benefit, the Courts have repeatedly had to permit the manual filing of return/claims and have directed the Department to act on such manual filing of returns. Accordingly, the Court issued a direction to the Department to either accept the manual return or alter the software to permit it to again file online its returns claiming the carry forward of losses of its ineligible unit for the AYs in question and either of these two options be completed by 31st May, 2019. Copy of the High Court order was also dispatched by the Registry to the Director General (Systems), Income Tax Department, New Delhi for compliance.

4. Reopening u/s 147 - (AY 2011 – 2012)

Best Cybercity (India) Pvt. Ltd. vs. ITO – WP(C) 12360/2018 & CM Appl. No.47877/2018, Delhi High Court, order dt.21-5-2019.

Assessee company was engaged in real estate development and related services. It filed its return of income for the AY in question on 29th September, 2011 declaring a loss of ₹ 22,534/-. The return was picked up for scrutiny and assessment order was passed u/s. 143(3) dt. 28-3-2013 after inquiring about various aspects. After four years, notice u/s. 148 dt. 29-3-2018 for reopening the assessment was issued. The record reasons stated that during the course of assessment proceedings of a sister concern of the Assessee i.e. Best International Projects Private Limited (BIPPL) for AY 2012-2013, it was noticed that a sum of ₹ 40 crores had been transferred from the account of PACL India Limited ('PACL') with Axis

Bank to the account of the Assessee. It was observed that PACL "is well known for giving and taking accommodating entries". The reasons further contained the analysis of the above information. According to the AO, the creditworthiness and genuineness of the above transaction remained unproved in the case of the Assessee in light of the financial position reflected in the returns and nature of the debit and credit entries reflected in the Bank account statements "in which transactions are squared up on daily basis or a day after day basis." The reasons further relied on the statement of one Shri Annu Aggarwal, Director of Assessee wherein it was clear that the Assessee had done no business activities ever since its incorporation and had no income for investment. It was further stated that the assessee had no business office premises either on rent basis or ownership basis. It had no fixed moveable assets and no staff to carry on day to day activities. It was then noted that Shri Aggarwal admitted not knowing the names of the Directors and Top Management officers of PACL which was well known for giving and taking accommodating entries. The name of PACL had been mentioned by one Shri Praveen Aggarwal a well known entry operator of Kolkata who had made a statement to that effect on 12th November, 2012 during search and seizure operation conducted at his group of companies. For the above reasons, the AO recorded that he had reason to believe that ₹ 40 crores received by the Assessee from PACL had escaped income for AY 2011-2012. The AO concluded that the Assessee had received "unexplained investment amounting Rs.40 crores" during the AY in question, which had escaped taxation which was due to the failure on the part of the Assessee disclosed fully and truly all material facts. On 24th October, 2018 the Assessee filed its objections to the re-opening of the assessment which were rejected by the AO by an order dated 26th October, 2018. The High Court observed that the requirement of the law in a case where the original assessment is under Section 143(3) of the Act and the re-opening of the assessment is beyond four years is well settled in a large number of cases which can be summarized as:

a) There must be tangible material that leads an AO to form reasons to believe that income chargeable to tax for the AY Year concerned has escaped assessment.

b) The AO's reasons must not be based on a mere change of opinion. Sections 147/148 of the Act cannot be invoked to overcome an oversight, inadvertent error and/or mistake in the original assessment order.

c) Where the original assessment is under Section 143(3) of the Act and is sought to be reopened beyond a period of four years from the end of the relevant AY, then in terms of the first proviso to Section 147 of the Act it must be additionally shown that the escapement of income was either on account of the Assessee's failure to file a return under Section 139, or in response to a notice under Sections 142(1) or 148 of the Act or failing to disclose fully and truly all material facts necessary for the assessment.

d) The reasons for re-opening the assessment must themselves contain all of the above elements. In other words the factum of the existence of tangible material and the recording of the satisfaction of the AO about the failure by the Assessee to disclose fully and truly all material facts necessary for the assessment must find place in the reasons recorded for re-

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> opening the assessment. The deficiency in this regard cannot be sought to be made up by a counter affidavit filed in the Court in response to a petition questioning the reopening of the assessment.

The Court observed that in the present case the detailed questionnaire was first issued on 23rd October, 2012 by the AO during the course of the original assessment proceedings under Section 143(3) of the Act. The AO had called for copies of all the bank accounts, the details of the sources of funds credited to the bank accounts and the application of the funds debited in such accounts. A reference was made to the search and seizure operations undertaken on 28th March, 2012 in which cash was found from plot No. H-8, Netaji Subhash Palace, New Delhi. On 30th October, 2012 the Assessee gave a point-wise reply including the Auditors report and the balance sheets, profit and loss account etc. By a separate letter dated 6th November, 2012 the Assessee give further clarifications on certain other points placed by the AO. A further notice was issued on 27th November, 2012 by the AO which was specific to the amount received from PACL. Copy of the agreement entered into with PACL Limited for development of IT park under joint venture with the best group and "details of amount of Rs.40 crores received from the parties during the year, along with documentary evidence" was also called for. On 25th January, 2013 the Assessee provided specific explanation. The certificate issued by the PACL limited stating that there is a balance of ₹ 40 crores in the name of the Assessee and the subsequent certificate dated 4th January, 2013 that debit balance is zero as on 31st March, 2012 was also furnished. The complete statement of bank account of Axis bank reflecting the debits and credits in the account including money received from PACL and repaid to it were furnished. It is therefore plain that all details pertaining to the amount received from PACL was in fact furnished by the Assessee to the AO. The Court held that, while, in the present case the assessment order does not itself discuss the details furnished by the Assessee, the fact remains that all the relevant materials were indeed disclosed by the Assessee before the AO. Also, the details of how the sum of Rs. 40 crores was disbursed appears to have been disclosed by the Assessee in a letter dated 2nd February, 2013 written by it to the AO in response to the questionnaire issued to it on 27th November, 2012. The Court therefore, held that all the material that was necessary for the AO to form an opinion regarding the transaction involving the Assessee and PACL was already available with the AO and there was no fresh tangible material on the basis of which the AO could have formed an opinion about any taxable having escaped assessment during the AY in question. Also, the reasons recorded by the AO for re-opening the assessment do not refer to the above facts. It merely repeats the language of Section 147 that there was a failure by the Assessee to disclose fully and truly all material facts necessary for the assessment. The Court was convinced that the jurisdictional requirement of the first proviso to Section 147 proviso has not been satisfied and hence it quashed the reopening notice and the order passed by the AO rejecting the objections raised by the Assessee to the re-opening of the assessment for the AY in question. The writ petition is accordingly allowed.

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

DIRECT TAXES

Tribunal

Unreported Decisions

1. Section 201(1) and 201(1A) – No order can be passed u/s. 201(1) & 201(1A) after expiry of one year from the end of the relevant financial year when the payments are made to the foreign entities

Atlas Copco (India) Limited vs. DCIT [ITA Nos: 1669, 1670 & 1671/PUN/2014]

DCIT vs. Atlas Copco (India) Limited [ITA Nos: 1685 to 1688/PUN/2014] & CO No: 60/PUN/2018 (Assessment Years: 2008-09 to 2011-12), Order dated 5-4-2019

Facts

In this case, the assessee is a Limited Company. During the assessment years under consideration, the assessee made payments to various foreign companies which are based in Canada, USA, UK, Belgium, Sweden, UAE and Hong Kong. The payments were made for procurement of software licence, software maintenance charges, testing charges, personal management fees etc. The assessee did not deduct TDS on the said payments. The Ld. AO therefore, issued a show cause notice to the assessee on 27-1-2012 u/s. 201(1) and 201(1A) of the Act asking it as to why the TDS was not deducted on the foreign remittance of ₹ 10,40,61,272/- for the A.Ys. 2008-09 to 2011-12. The said query of the Ld. AO was replied by the assessee. The Ld. AO further, passed the common order for the A.Ys. 2008-09 to 2011-12, dated 6-2-2014 u/s. 201(1) & 201(1A) of the Act and held that the payments made by the assessee are in the nature of royalty/fee for technical services u/s. 9(1)(vi) and 9(1)(vii). Thus, the TDS was required to be deducted on the same. Pursuant to the same, the Ld. AO raised the total demand of ₹ 1,81,06,064/- i.e. TDS plus interest for non-compliance of the provisions of Chapter XVII-B of the Act. On appeal, the Ld. CIT (A) partly allowed the appeals of the assessee. Being aggrieved by the appellate order, both assessee and Department went in appeals before Hon'ble ITAT. The assessee filed additional legal ground before Hon'ble ITAT, challenging that the order dated 6-2-2014 passed u/s. 201(1) & 201(1A) is barred by limitation. Thus, the same is null and void. Before Hon'ble ITAT, the assessee explained that the notice initiating the proceedings u/s. 201(1) of the Act was issued on 27-1-2012. However, the order u/s. 201(1) & 201(1A) was passed by the Ld. AO on 6-2-2014 that

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is much beyond the reasonable time. The assessee placed reliance on the decision of Special Bench in the case of *M/s. Mahendra and Mahendra Ltd. vs. DCIT 122 TTJ 577 (Mum)(SB)* to support its contentions and explained that Hon'ble Special Bench, ITAT Mumbai in the said decision has held that the proceedings u/s. 201(1) are akin to 'Assessments' and the 'Assessments' includes 'Reassessments'. Thus, the order u/s. 201(1) of the Act has to be passed within the time limit prescribed u/s. 153(2) of the Act. Accordingly, the order u/s. 201(1) needs to be passed within one year from the end of the financial year in which the proceedings u/s. 201(1) are initiated. On the other hand, the Ld. DR after relying on the provisions of section 201(3) of the Act submitted that the order u/s. 201(1) of the Act can be passed at any time after the expiry of six years from the end of the financial year in which payments are made or credit is given to the payee. Thus, Ld. DR contended that the order u/s. 201(1) is passed within the time provided u/s. 201(3) of the Act. After hearing both the parties, Hon'ble ITAT came to the following conclusion.

Held

After considering the submissions of the parties, Hon'ble ITAT observed that the provisions of section 201(3) of the Act can be attracted only where the assessee fails to deduct TDS on the payments made to a person resident in India. In the present case, the payments were made to the foreign entities and the said fact is accepted by the Ld. AO in the assessment order itself. Thus, the provisions of section 201(3) cannot apply in the present case. Hon'ble ITAT referring to the decision of Special Bench in case of Mahendra & Mahendra (Supra) has observed that the proceedings u/s. 201(1) are similar to the Assessment and the Assessment includes Reassessment. Thus, no order u/s. 201(1) can be passed after expiry of one year from the end of the relevant assessment year. In the present case, the proceedings u/s. 201(1) for all the years under consideration were initiated *vide* notice dated 27-1-2012 and a common order dated 6-2-2014 was passed u/s. 201(1) & 201(1A) of the Act. The same is beyond the reasonable time prescribed u/s. 153(2) of the Act. Thus, Hon'ble ITAT came to the conclusion that the order passed u/s. 201(1) is void *ab initio* and the appeals of the assessee were allowed on the legal ground.

2. Method of accounting – Assessing officer cannot go beyond the method of accounting consistently followed by the assessee and tax the same income which has already been taxed in the earlier year

ACIT vs. PHE Consultants [ITA 6943/Mum/2017] (Assessment Year: 2012-13) order dated 24-05-2019

Facts

In this case, the assessee is a Partnership Firm, engaged in the business of providing consultancy services in the environment sector. The return for the year under consideration was filed on 29-9-2012 declaring the total income at ₹ 10,66,930/-. During the course of scrutiny assessment, the Ld. AO observed that the assessee debited an amount of ₹ 1,98,75,000/- in the Profit and Loss Account as fees receivable. The Ld. AO was of the opinion that amount receivable cannot be debited as expenditure since it is a revenue receipt which should have been shown in the credit side of the Profit & Loss Account. Accordingly, the Ld. AO made a disallowance of ₹ 1,98,75,000/- treating the same as income of the assessee. The appeal was preferred before Ld. CIT (A) challenging the action of the Ld. AO. The Ld. CIT(A) allowed the appeal by observing that the assessee has been following work

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completion method consistently. As per the method of accounting, the Assessee offered an amount of ₹ 1,98,75,000/- in the A.Y. 2011-12 on estimation basis. He further, approved the method of accounting followed by the Assessee on the observation that it has been consistently followed. The Revenue being aggrieved by the order passed by Ld.CIT(A) preferred an appeal before Hon'ble ITAT. After hearing both the sides, Hon'ble ITAT held as under:

Held

Hon'ble ITAT observed that the assessee renders services to BMC. As per the system of accounting followed by the assessee, at the end of each accounting year it estimates the extent of work done and makes the provision for fees receivable in the books of accounts which is offered to tax. Accordingly, the assessee offered the income of ₹ 1,98,75,000/- in the immediately preceding assessment year (i.e., A.Y. 2011-12). The said provision was reversed in the subsequent assessment year i.e., in A.Y. 2012-13 and claimed as an expenditure to avoid double taxation. Hon'ble ITAT further, held that the assessee is following this method of accounting since its inception of business. It is also held that the assessee has already offered/considered the fees receivable as income in the assessment year 2011-12 and the opening balance of fees receivable was claimed as expenditure in the A.Y. 2012-13. Hon'ble ITAT observed that the Ld. A.O. is taxing the same income once again in the year under consideration which has already been considered for tax in the A.Y. 2011-12 and the same is impermissible under the law. Hon'ble ITAT further, referring to the decision of Hon'ble Bombay High Court in the case of *PCIT vs. C.U. Inspections India Pvt. Ltd. [2018] 91 taxmann.com 344 (Bom)* held that bringing the same amount to tax once again in the impugned assessment year which has already suffered taxation in the earlier year would result in double taxation. In view of the same, Hon'ble ITAT confirmed the observation of the Ld. CIT(A) and dismissed the appeal of the Revenue.

Reported Decisions

3. Section 54F: While the computing number of houses owned by an assessee for the purpose of a deduction u/s. 54F, the jointly owned property is to be excluded

Ashok G. Chauhan v. ACIT [ITA: 1309/Mum/2016] (Assessment Year: 2010-11) order dated 12-04-2019- (2019) 105 taxmann.com 204 (Mum)(Trib.)

Facts

The assessee filed his return of income claiming a deduction u/s. 54F in respect of capital gain arising from the transfer of the capital asset. During the course of the assessment proceedings, the Ld. AO observed that at time of transfer of a capital asset, the assessee was the owner of two residential houses out of which one he had jointly purchased with his wife and therefore he rejected the claim for deduction on the ground that the Assessee was the owner of two flats on date of transfer of capital assets. Being aggrieved by the same, the Assessee preferred an appeal before the Ld. CIT(A) but did not succeed. Thereafter, an appeal was filed before Hon'ble ITAT. After hearing both the parties, Hon'ble ITAT held as under:

Held

At the outset, Hon'ble ITAT observed that it is an undisputed fact that assessee was actually co-owner of the property i.e., flat at Goa along with his wife and had transferred his share to his daughter by virtue of gift deed dated 15-4-2004. It was further observed that the assessee did not fully own the said flat at Goa. Thereafter, Hon'ble ITAT perused the provisions of Section 54F of the Act and noted that the legislature has used the word 'a' before the words 'residential house'. It must mean a complete residential house and would

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not include a shared interest in a residential house. Where the property owned by more than one person, it cannot be said that any one of them is the owner of the property. No individual person of his own can sell the entire property. No doubt, he can sell his share of interest in the property but as far as the property is considered, it would continue to be owned by co-owners. Joint ownership is different from absolute ownership. In the case of residential unit, none of the co-owners can claim that he is the owner of residential house. Ownership of a residential house means ownership to the exclusion of all others. Therefore, where a house is jointly owned by two or more persons, none of them can be said to be the owner of that house. So, the word "own" would not include a case where a residential house is partly owned by one person or partly owned by other persons. While adopting the abovementioned view, Hon'ble ITAT relied on the decision of Hon'ble Apex Court in the case of *"Seth Banarsi Dass Gupta vs. CIT [1987] 166 ITR 783"*. Finally, Hon'ble ITAT accepted the contention of the Assessee and directed the Ld. AO to allow a deduction of Sec 54F of the Act.

4. Section 115JA- When an assessee being a banking company is required to maintain books of account as per the Banking Regulation Act, 1949 and not as per the Companies Act, 1956, Section 115JA has no applicability in such a case

Standard Chartered Bank vs. JCIT [ITA: 7891 & 9229/Mum/2004] (Assessment Year: 1997-98) order dated 12-4-2019- (2019) 104 taxmann.com 236 (Mum)(Trib.)

Facts

The assessee in the present case is a foreign company incorporated by the Royal Charter under the laws of England and Wales. It carries on business of banking, financial service and allied activities. With the permission of Reserve Bank of India, the assessee opened branches and carried on the banking business in India. During the course of assessment proceedings for the assessment years 1999-2000 and 2005-06, the Ld. AO invoked the provisions of Section 115JA of the Act. Being aggrieved by the same, the assessee carried out the matter to the first appellate authority but did not find any success. Thereafter, an appeal was preferred before Hon'ble ITAT. During the course of the hearing, it was submitted before Hon'ble ITAT that the assessee being a banking company is not required to maintain its account as per the provisions of the Companies Act, 1956 and thus section 115JA is not at all applicable to the facts under consideration. To buttress the submission, the Assessee relied upon various case laws which were laid down regarding the applicability of Section 115JB to the assessees to whom the provisions of Companies Act were not applicable. On the other hand, the Ld. DR vehemently opposed the contentions of the assessee. After hearing both the sides, Hon'ble ITAT held as under:

Held

Hon'ble ITAT perused the provisions of Section 115JA of the Act and the relevant case laws cited by the assessee. It observed that the assessee being governed under the Banking Regulations Act, 1949, is not required to prepare its Profit & Loss Account under the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. That being the case, the provisions of section 115JA of the Act are not applicable to the assessee. While coming to the aforesaid conclusion, Hon'ble ITAT referred to the decision of its co-ordinate benches and accepted the contention of the assessee.

Note: Decision pertains to the provisions of Act as applicable prior to the amendment made w.e.f. 1-4-2012.

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INTERNATIONAL TAXATION
Case Law Update

A. HIGH COURT

1. Where the entire TP adjustment hinged only on one comparable and difference in functionality of assessee and said comparable was not discussed by Tribunal, entire issue of determining TP adjustment was to be considered afresh by TPO

Pyramid IT Consulting vs. Add. CIT [(2019) 105 taxmann.com 281 (Delhi HC)] - W.P. (C) 5198/2019

Facts

1. The assessee, engaged in the business of providing value added IT Solutions and IT staffing services to global companies, had selected two comparables having average margin of -18.07% while benchmarking the services rendered to its AE under the staffing segment.

2. The TPO rejected both the comparables and introduced another comparable i.e., HCCA Business Services Pvt. Ltd. (HCCA) having margin of 20.05% as against the assessee's margin of 2.46% and made an adjustment accordingly. The DRP as well as the Tribunal upheld the order of the TPO rejecting assessee's contention that HCCA was functionally different and thus not comparable.

3. The Tribunal also rejected the Miscellaneous Application (MA) filed by the assessee u/s. 254(2) against its own order, wherein the assessee had contended that (i) though the Tribunal had noted in its order that HCCA owned 'intangibles', yet it was not excluded as a comparable (ii) though the assessee had relied/placed before the Tribunal, the decision of the Tribunal in the case of *LG Chemicals India Pvt. Ltd. vs. ACIT* where the same comparable i.e., HCCA was excluded holding it to have a different functional profile from the assessee in that case, the said decision was not even discussed by the Tribunal in its order.

4. Aggrieved, the assessee filed a Writ Petition before the High Court against the Tribunal's order dismissing the MA.

Held

1. The Court noted that there was no discussion by Tribunal of its earlier order in LG Chemicals India Pvt. Ltd. where it was held that a company owning intangibles could not be compared with one which does not.

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2. Further, noting that the Tribunal had not discussed the difference in functionality of the assessee and HCCA, whereas the entire TP Adjustment has hinged only on one comparable, it held that Tribunal had overlooked assessee's objections against inclusion of HCCA (which according to the assessee was only providing payroll processing services as against staffing services provided by the assessee) and thus the same required a detailed consideration.

3. Accordingly, the Court allowed the assessee's writ petition and remanded the matter back to the TPO stating that the entire issue of determining the TP adjustment in respect of the transactions in the staffing segment should be considered afresh by the TPO uninfluenced by his earlier order.

2. Genesys International Corporation Ltd., engaged in providing diverse operations providing high-end and complex services, is not comparable to an entity providing only back office IT enabled services

CIT vs. EXL Services.com India Private Limited [TS-437-HC-2019 (Delhi)] - ITA 487 of 2019.

Facts

1. The assessee, a wholly owned subsidiary of EXL Service Holdings, was engaged in rendering business and knowledge process outsourcing, research and analysis and risk advisory (known as IT Enabled Services) for customers of the EXL group entities.

2. The assessee had selected 14 comparable while benchmarking the aforesaid services, out of which the TPO accepted 9 comparables and added 2 more comparables, thus arriving at a final set of 11 comparables whose average margin was 22.26% as against assessee's margin of 7.14%. Accordingly, he proposed an adjustment.

3. The assessee filed its objections before the DRP which *inter alia* accepted assessee's submission that Genesys International Corporation Ltd. (GICL) should be omitted from the list of comparables since the same was not functionally similar to the assessee. Accordingly, while passing the final assessment order pursuant to the DRP directions, the AO deleted the earlier proposed said adjustment.

4. The Revenue being aggrieved by the said order of the AO, filed an appeal before the Tribunal which upheld the DRP's direction and consequently the final assessment order passed by the AO.

Held

1. The Court noted that GICL was engaged in diversified operations providing high-end and complex services such as GIS Consulting, 3D Mapping, Navigation Maps, Remote Sensoring, etc., whereas the assessee was engaged only in providing back office IT enabled services.

2. Further, GICL operated as a full-fledged risk taking entrepreneur whereas the assessee was not. Therefore, apart from the functionality aspect, the comparison failed even on the basis of the scale of risk.

3. From the Annual Report of GICL, it was noticed that it had significant intangibles in the form of computer software and GIS data base whereas the assessee did not own any significant intangibles. It depended entirely on the intellectual property rights owned by the holding company.

4. Thus, the Court dismissed Revenue's appeal and held that no substantial question of law arose.

3. The Court directed the AO to issue certificate of no requirement of deducting tax at source under

section 197 with respect to capital gains earned by the Mauritian Entity on sale of shares of an Indian company on a *prima facie* view that the said gains was not taxable in India in view of Article 13 of the India-Mauritius DTAA. Also, directed the Revenue to release the TDS amount already deposited by the deductor with the Government subject to security amounting to 200% of disputed tax amount

Indostar Capital vs. Asst. Commissioner of Income Tax [TS-250-HC-2019 (Bombay)] - Writ Petition No. 3296 of 2018

Facts

1. The assessee-company, which was issued the Tax Residency Certificate (TRC) by Mauritius Revenue Authority, owning 7.13 crore (rounded off) shares of IFCL (Indian NBFC) which was 97.30% of its share capital, desired to offload some 1.85 crore (rounded off) of its shares of IFCL.

2. The assessee applied to the AO for grant of the certificate under section 197 of the Act making detailed averments as to why income (i.e., capital gains arising on sale of shares) receivable by it was not chargeable to tax as per the India-Mauritius DTAA. However, the AO rejected the application for certificate, holding that the transaction was not genuine and the entire tax structure was created to avoid legitimate tax liability arising in India.

3. Further, during course of proceedings, in absence of above certificate being issued in favour of the assessee, the payer deducted the relevant amount of TDS and deposited the same with the Government.

4. Aggrieved, the assessee filed a writ petition before the Court to challenge the order rejecting the application for certificate under section 197 as well as praying for refund of the amount deposited by the payer.

Held

1. The Court held that as per Article 13(4) of the India-Mauritius DTAA as it stood at the relevant time, the capital gains arising out of the sale of shares of Indian company acquired on or before 31-3-2017 could be taxed, if at all, in Mauritius i.e., it could not be taxed in India.

2. It relied on the decision in the case of *CIT(IT) vs. JSH (Mauritius) Ltd.* wherein it was held that when the assessee had placed reliance on DTAA between two countries, reference to section 9(1)(i) and *Explanation* 5 thereto would be of no relevance. The Court also took note of the CBDT Circular which had clarified that TRC will constitute sufficient evidence for accepting status of the residence as well as beneficial ownership for applying the DTAA.

3. Further, noting that the AO did not have any sufficient *prima facie* material to demonstrate that the entire transaction from the inception was sham, colourable device and a bogus transaction to simply avoid tax, it held that mere fact that the assessee-company had not transacted any other business by itself may not be conclusive proof to accept AO's contention. It held that the extent of administrative expenditure and the employment structure may be some of the factors which eventually would go to establish whether the transaction was sham and the very existence of the assessee was fraudulent, however by themselves they may not be sufficient. Further, it held that all these aspects could and need to be gone into in the assessment proceedings.

4. Accordingly, the Court (i) quashed the order rejecting the application filed by the assessee (ii) directed the AO to issue certificate under section 197 stating that there is no requirement to deduct TDS (iii) gave direction to release the TDS amount already deposited by the payer.

5. Further, taking note of Revenue's anxiety to protect recovery of taxes, it also directed the assessee to continue to hold minimum 50 lakh shares of ICFL (having valuation of 200% of the disputed tax amount) till the last day of passing the assessment order for the relevant year (unless the said order is passed before such date).

6. Accordingly, the writ petition was disposed of.

4. TPO erred in recharacterising the assessee from a business support service provider to a trader and further erred in including the FOB value of goods sourced from India for its AEs in the operating cost of the assessee to compute the assessee's margin while adopting TNMM

Pr.CIT vs. M/s. Itochu India Private Limited [TS-428-HC-2019 (Delhi)] - ITA Nos. 1111, 1129 & 1130 of 2018

Facts

1. The assessee was in the business of rendering support services in relation to facilitation and market support to its AEs in order to facilitate sourcing transactions of its AEs with prospective sellers. As per the TP study, the assessee's margin (*viz.*, 110.91%, 123.52% & 129.34% for AY 2007-08, AY 2008-09 & AY 2009-10 respectively) was higher than the mean of comparables margin (*viz.*, 15.29%, 15.28% & 14.05% for AY 2007-08, AY 2008-09 & AY 2009-10 respectively).

2. The TPO recharacterised the business profile of the assessee from a business support service provider to a trader and included the Free on Board (FOB) value of goods sourced from India in the operating cost of the assessee to compute the assessee's margin for benchmarking using TNMM. He conducted a fresh search identifying trading companies as comparable to assessee and made an adjustment with respect to business support services rendered by the assessee to its AEs, considering average margins of such trading companies.

3. The assessee filed appeal before CIT(A) which held that the assessee was engaged in the business of rendering business support services and was not a trader. Further, it held that the FOB value of goods sourced by AEs could not be included in the cost of the assessee for computing the assessee's margin. The CIT(A) also accepted the comparables selected by the assessee in its TP study and held that the assessee's international transactions were at arm's length.

4. The Tribunal also upheld the CIT(A)'s order.

5. Aggrieved Revenue had filed appeal against Tribunal's order.

Held

1. The Court relied on the decision in the case of *Li & Fung India Pvt. Ltd. vs. CIT (2014) 361 ITR 85 (Del)* wherein it was held that to apply TNMM, assessee's net profit margin realized from the international transactions had to be calculated only with reference to the cost incurred by itself and not by any other entity i.e., third party vendors or AEs. Thus, it held that including the FOB value of AE's contract in the operating cost of the assessee in order to determine its margin was not sustainable in law.

2. It held that the Tribunal had rightly held that the TPO had artificially enhanced the cost base of the taxpayer and proposed a mark-up of the FOB value of goods sourced by AEs and as such this approach was not available in TNMM as per Rule 10B(1)(e) of the Income-tax Rules.

3. Further, it held that the Tribunal's observation that the TPO "had wrongly

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recharacterised the business function of the taxpayer from a business support service provider to a trader" also did not suffer from any legal infirmity.

4. Accordingly, the Revenue's appeal was dismissed.

B) Tribunal Decisions

I) Tribunal upholds assessee's claim of split-residency based on Article 4 of the India-USA tax treaty

DCIT vs. Shri Kumar Sanjeev Ranjan [TS-191-ITAT-2019 (Bang)]

Assessment year : 2013-14

Facts

i) The assessee, a US citizen, was on a temporary cross-border assignment to India, from June 2006 until 10th August, 2012, and thereafter, repatriated to the USA with his family.

ii) For the financial year (FY) 2012-13 (assessment year 2013-14), the assessee was a Resident and Ordinarily Resident (ROR) of India and resident of the USA under the domestic tax law of the respective countries.

iii) For FY 2012-13, the assessee filed his tax return and declared his total income after claiming the exemption under Article 16(1) of the tax treaty for the salary income earned for the period 11th August, 2012 to 31st March, 2013.

iv) During the assessment proceedings, the Tax Officer (TO) asked the assessee to submit his residential status, legal position on split residency and exemption under Article 16(1) of the tax treaty for the salary income earned for the period 11th August, 2012 to 31st March, 2013.

v) The assessee contended that in case an individual is a resident of both contracting states of the tax treaty, the residential status of the individual needs to be determined in accordance with Article 4(2) of the tax treaty (tie-breaker rules).

vi) For the period 1st April, 2012 to 10th August, 2012, since the house property of the assessee in the USA was let-out, for the purpose of the tie-breaker, the house will be considered as "unavailable for use" to the assessee during this period. Hence, he satisfied the first test for "availability of permanent home" in India and tie-broke his residency to India for this period.

vii) For the period 11th August, 2012 to 31st March, 2013, since there was a tie in the first test of tie-breaker rules under the tax treaty (availability of permanent home in both contracting states), the second tie-breaker test "centre of vital interest" needs to be looked into.

viii) Based on the following facts, the assessee contended that for the period 11th August, 2012 to 31st March, 2013, he tie-broke his residency to the USA, as his centre of vital interests was in the USA:

- He and his dependent members (his wife and two children) are citizens of the USA and repatriated to the USA with him after 10th August, 2012;
- He has two house properties, car and all other personal belongings in the USA;
- He has voting rights in the USA;
- He holds a driving license in the USA;
- His designated country of residence is the USA, and he has filed Virginia state tax returns, as Virginia was his home;
- He has all his investments (in shares, mutual funds, 401k and insurance policies) in the USA and contributes to the social security plans of the USA; and

- His habitual abode is in the USA for the following reasons:
  - He has been working for USA-based companies in the USA;
  - He is contributing towards the USA social security since 1988;
  - He is a citizen of the USA since 1992;
  - He is paying taxes in the USA since 1988;
  - His spouse and children are continuously residing with him in the USA;
  - His children are born in the USA;
  - He spends summer vacations in the USA;
  - He has spent an aggregate of 30 years in the USA; and
  - He has plans to stay in the USA for the rest of his lifespan with his spouse and children.
- The TO contended that the personal and economic relations refer to a long and continuous relation that an individual nurtures with a place. Therefore, the assessee cannot claim that after the end of his assignment (i.e., from 11th August, 2012) his economic and personal relations were suddenly closer to the USA than India.
- There is no concept of split residency under the provisions of the Indian Income-tax Act, 1961 or the tax treaty.
- The assessee did not satisfy the conditions for claiming exemption under the tax treaty, as he did not furnish the Tax Residency Certificate (TRC) or the Form 10F.
- In view of the above, the TO added the assessee's global income earned during the period 11th August, 2012 to 31st March, 2013 to his total income.
- The assessee submitted the TRC before Commissioner of Income-tax (Appeal) [CIT(A)] for the years 2012 and 2013 obtained from the USA tax authorities.
- CIT(A) held that as the assessee had a permanent home available to him in both India and the USA for the period 11th August, 2012 to 31st March 2013, there was a tie in the first test of the tie-breaker rules under Article 4(2)(a) of the tax treaty.
- Based on the facts presented before the CIT(A) (mentioned supra), it was concluded that by applying the second tie-breaker test, the assessee has established that his centre of vital interests (personal and economic relations) was closer to the USA, and therefore, he was a resident of the USA for the period 11th August, 2012 to 31st March, 2013.
- Since the assessee's residency tie-breaks to the USA under the tax treaty, the exemption is available to him.

Tribunal's decision

- The Tribunal held that the CIT(A)'s conclusion on determining the residential status of the assessee under the tax treaty was not based on the TRC, but on the test of his personal and economic relations (centre of vital interests) under Article 4(2) of the tax treaty.
- The Tribunal agreed with the conclusion of the CIT(A) on the basis of the facts presented by the assessee before the CIT(A).

II) Companies for which data is not available in the public domain can be selected by the Transfer Pricing Officer as comparables

by using their power to call for information under Section 133(6) of the Income-tax Act.

Philips Medical Systems (P.) Ltd. vs. ITO [2019] 102 taxmann.com 441 (Kol.)

Facts

- The assessee is a distributor and commission agent for medical equipment in India. During the year it has imported equipment and spares for distribution from its associated enterprise (AE). It has also received commission income from its AE. The assessee justified the arm's length nature of transactions by application of Transactional Net Margin Method at entity level. The assessee used 10 comparable companies and operating profit to sales as the profit level indicator.
- The Transfer Pricing Officer (TPO) however rejected all the comparable companies selected by the assessee (providing reasons such as substantial related party transactions, functional comparability, low turnover, etc.). The TPO selected two comparable companies for which data was not available in the public domain.
- Upon appeal, the CIT(A), while reducing the adjustment by accepting 5 out of 10 comparable companies of the assessee, also held that restriction to use publicly available data does not apply to the AO. Hence the two comparable companies selected by the TPO were also accepted resulting in selection of seven comparable companies including two selected by the TPO.
- Cross appeals were filed both by the assessee as well as the department.

Tribunal's decision

i) The Tribunal upheld the decision of the CIT(A) that the restriction stipulated in Rule 10D is applicable only to the auditor and not to the TPO, who has an inherent power to make enquiry and collect and use the information and material which is found to be relevant for the purpose of transfer pricing analysis in order to determine the arm's length price of the relevant international transactions between the AE.

ii) The Tribunal rejected a comparable engaged in manufacturing as well as trading activity in the absence of segmental details as it is not functionally comparable to the assessee which is mainly engaged in trading activity.

III) Multiple counting and period of leave is to be excluded from the period of stay of an employee to determine Service PE threshold

Linklaters vs. DDIT [TS-210-ITAT-2019 (Mum)]

Assessment Year : 2002–03

Facts

i) The assessee, a partnership firm, is a tax resident of United Kingdom (U.K.) and is engaged in the practice of law. Apart from its head office in the U.K., the assessee has offices in various other countries around the world. The assessee does not have any branch office in India. The assessee was appointed as a legal advisor for some of the projects in India and provided legal consultancy services to them. In connection with rendering such legal consultancy services, the assessee received fees from the clients in India.

ii) The assessee filed its return of income for the Assessment Year (AY) 2002-03 on 31st October, 2002, declaring nil income. The statement accompanying the return of income stated that since the assessee had no branch office in India, the fee received is not chargeable to tax in India in the absence of a PE in India.

iii) The Assessing Office (AO) observed that the employees/other personnel of the assessee have rendered services in India for more than

90 days during the relevant financial year, hence, the assessee had a PE in India in terms of Article 5(2)(k)(i) of the tax treaty. Therefore, income earned from rendering legal consultancy services in India is taxable in India.

Decision

i) The only issue that is required to be examined is, whether the employees/other personnel of the assessee have stayed and rendered services in India during the relevant financial year exceeding the period of 90 days to constitute a PE in India.

ii) In this context, the assessee had contended that (a) if the vacation period of one of the employees Shri Narayan Iyar (said employee) is excluded, the period of stay of the employees of the assessee in India would be 87 days and (b) multiple counting of employees in a single day is not permitted.

iii) The said employee had not rendered any services in India from 17th April, 2001 to 4th May, 2001, as he was availing a study leave and therefore, the same period has to be excluded for computing the period of 90 days as no other employee of the assessee was rendering services in India.

iv) The next issue which requires consideration is, whether multiple counting of employees on a single day is permissible. A careful reading of Article 5(2)(k)(i) of the tax treaty makes it clear that as per the expression used therein if the employees or other personnel have stayed in India for a period exceeding 90 days in any 12 month period, it will constitute a PE. In the facts of the present case, the AO had reckoned any 12 month period to be the financial year beginning from 1st April, 2001 to 31st March, 2002.

v) Therefore, the stay of employees in India on a particular day has to be taken cumulatively and not independently. That being the case, multiple counting of employee in a single day, as was done by the tax authorities, is not impermissible under Article 5(2)(k)(i) of the tax treaty. The Tribunal referred to the decision of the Mumbai Tribunal in the case of *Clifford Chance vs. DCIT [2002] 82 ITD 106 (Mum)*, relied upon by the assessee.

vi) Thus, if the period during which the said employee was on leave is excluded and the multiple counting of employees in a single day is avoided, the aggregate period of stay of assessee's employees' in India during the relevant financial year is 87 days.

vii) Therefore, there was no PE of the assessee in India during relevant assessment year. That being the case, the fees received by the assessee from legal consultancy services rendered in India is not taxable in India.

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INDIRECT TAXES

GST Gyan

Valuation Rules under GST

In any taxation law, measure is an important element of levy. In the absence of valuation, levy may fail. The charging section, therefore clearly provides that the levy shall be on the value determined under section 15. Section 15 of the CGST Act provides that the value shall be the "transaction value". A transaction value shall be taken to mean the price actually paid or payable for the said supply of goods or services or both where the supplier and the recipient of the supply are not related and the price is the sole consideration for the supply. In cases where, the price actually charged to the receiver does not correspond to the attributes of transaction value, then the Valuation Rules, come into picture. This article compiles valuation rules, available in GST law, applicable in various circumstances.

1. Chapter IV of the CGST Rules deal with Determination of Value of Supply. The summary of situations covered in the said Rule is as under:

    - Rule 27 - Value of supply of goods or services where the consideration is not wholly in money.

    - Rule 28 - Value of supply of goods or services or both between distinct or related persons, other than through an agent.

    - Rule 29 - Value of supply of goods made or received through an agent.

    - Rule 30 - Value of supply of goods or services or both based on cost

    - Rule 31 - Residual method for determination of value of supply of goods or services or both.

    - Rule 31A - Value of supply in case of lottery, betting, gambling and horse racing

    - Rule 32(2) – The value of supply of services in relation to the purchase or sale of foreign currency, including money changing.

    - Rule 32(3) - The value of the supply of services in relation to booking of tickets for travel by air.

    - Rule 32(4) - The value of supply of services in relation to life insurance business.

    - Rule 32(5) - Where a taxable supply is provided by a person dealing in

buying and selling of second hand goods

- Rule 32(6) - The value of a token, or a voucher, or a coupon, or a stamp

2. Rule 27 is applicable in cases where the supply is for a consideration which is either wholly in non-monetary form or partly in monetary and partly in non-monetary form. The rule provides the parameters to be adopted for arriving at value of non-monetary consideration. Rule 27 provides that, such value shall be the 'open market value'. The concept of "open market value" suggest a value from the view point of a receiver in an independent transaction (i.e., transaction with unrelated party) at the same time when the supply being valued is made. Where "open market value" is not available, the value for supply of like kind and quality can be taken as a base. In simple words, the law permits adopting value of similar goods (closely or substantially resembles in respect of the characteristics, quality, quantity, functional components, materials, and the reputation of the goods or services being supplied) as transaction value. If both these methods fail, then value shall be determined in accordance with the general principles contained in sections 30 and 31. Section 30 adopts cost of goods and services being supplied as a base and deems 110% of the cost of production or manufacture or the cost of acquisition of such goods or the cost of provision of such services, as the value. However as regards provision of services, instead of this rule, the supplier may determine the value as per residuary rule contained in section 31 i.e., using reasonable means consistent with the principles and the general provisions of section 15.

3. Para 2 of Schedule 1 of CGST Act provides for supply of goods or services or both without consideration, between related persons or between distinct persons as specified in section 25, as deemed supply, when made in the course or furtherance of business. Rule 28 provides for valuation of the same. The valuation shall be done using principles similar to those explained in Rule 27 above. However, two additional options are provided for such type of transaction as under:

   i. where the goods are intended for further supply as such by the recipient to an unrelated buyer, the value shall, be an amount equivalent to 90% of the price charged for the supply of goods of like kind and quality by the recipient to his customer. Here the price is decided from the view point of the receiver leaving him margin of 10% on sale. The rule is applicable only in respect of goods.

   ii. where the recipient is eligible for "full" input tax credit, any value declared in the invoice shall be deemed to be the open market value of the goods or services. It's to be noted that, "eligibility of ITC" is to be seen from the goods/services being supplied. Hence, where the goods or services being supplied are to be used by the receiver partly for making taxable supplies and partly for making exempt supply, the recipient may not be said to be eligible for "full" input tax credit due to provisions of Rules 42 and 43 of the CGST Rules and therefore in such cases, this option may become unworkable. However, where the goods/services supplied are directly attributable to further supply of taxable goods/services, this option will find its utility.

4. Rule 29 deals with supply of goods made or received through agents. The valuation is either open market value or 90% of the price charged for the supply of goods of like kind and quality by the recipient to his unrelated customer.

5. **Lottery, betting and gambling (Rule 31A)**

In case of supply of lottery the value of supply of lottery ***run*** by State Governments shall be deemed to be 100/112 of the face value of ticket or of the price as notified in the Official Gazette by the organising State, whichever is higher. The value of supply of lottery ***authorised*** by State Governments shall be deemed to be 100/128 of the face value of ticket or of the price as notified in the Official Gazette by the organising State, whichever is higher.

The value of supply of actionable claim in the form of chance to win in betting, gambling or horse racing in a race club shall be 100% of the face value of the bet or the amount paid into the totalisator.

6. **In case of supply of services in relation to the purchase or sale of foreign currency, including money changing, there are two options:**

Option 1

(a)	for a currency, when exchanged from, or to, Indian Rupees -		(buying rate or the selling rate, as the case may be) **Less** (the Reserve Bank of India reference rate for that currency at that time) **multiplied by** the total units of currency. Provided that in case where the Reserve Bank of India reference rate for a currency is not available, the value shall be one per cent. of the gross amount of Indian Rupees provided or received by the person changing the money.
(b)	where neither of the currencies exchanged is Indian Rupees		Lower of the Following
		(i)	1% of the (Currency bought x RBI Reference Rate)
		(ii)	1% of the (Currency sold x RBI Reference Rate)

Option: 2

If this option is exercised for a financial year and such option shall not be withdrawn during the remaining part of that financial year.

Gross Amount of Currency Exchanged		*Value*	
(a)	Up to ₹ 25,000	₹ 250	
(b)	₹ 25001 to ₹ 1,00,000	1% of the gross amount of currency exchanged.	
(c)	₹ 1,00,001 to ₹ 10,00,000	₹ 1,000 + 0.5% x (gross amount of currency exchanged – ₹ 1,00,000)	
(d)	₹ 10,00,001 and above		Lower of the following:
		(i)	₹ 5,500 + 0.1% x (gross amount of currency exchanged – ₹ 10,00,000)
		(ii)	₹ 60,000

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For arriving at "gross amount of currency exchanged", exchange rate shall be taken as per section 34(2) i.e., the applicable rate of exchange determined as per the generally accepted accounting principles for the date of time of supply of such services in terms of section 13 of the Act.

7. **The value of the supply of services in relation to booking of tickets for travel by air provided by an air travel agent shall be computed as under:**

(a)	Domestic bookings	5% of the Basic Fare
(b)	International Bookings	10% of the Basic Fare

The expression — "basic fare" means that part of the air fare on which commission is normally paid to the air travel agent by the airlines.

In cases where no commission is paid, "basic fare" may be determined as per prevalent industry practices (i.e. the fare adopted by such airlines for paying commission to other agents in the industry)

8. **The value of supply of services in relation to life insurance business shall be computed as under:**

(a)	Scenario - 1	the gross premium charged from a policy holder (less) the amount allocated for investment, or savings on behalf of the policy holder, [if such an amount is intimated to the policy holder at the time of supply of service]
(b)	Scenario - 2	in case of single premium annuity policies other than (a) 10% of single premium charged from the policy holder.
(c)	Scenario - 3	in all other cases, First Year Premium - 25% of the premium charged Subsequent Years - 12.5% of the premium charged.

Where the entire premium paid by the policy holder is only towards the risk cover in life insurance, the said value shall be ignored.

9. **Dealer in second hand goods where No ITC is availed**

Where a taxable supply is provided by a person dealing in buying and selling of second hand goods i.e., used goods as such or after such minor processing which does not change the nature of the goods and where no input tax credit has been availed on the purchase of such goods, the value of supply shall be the difference between the selling price and the purchase price and where the value of such supply is negative, it shall be ignored. Hence, in case the value is negative, it shall be taken as NIL.

10. **Value in case of goods repossessed from unregistered defaulting borrower**

The purchase value of goods repossessed from an unregistered defaulting borrower, who is not registered, for the purpose of recovery of a loan or debt shall be deemed to be the purchase price of such goods by the defaulting borrower reduced by five percentage

points for every quarter or part thereof, between the date of purchase and the date of disposal by the person making such repossession.

11. The value of a token, or a voucher, or a coupon, or a stamp (other than postage stamp) which is redeemable against a supply of goods or services or both shall be equal to the money value of the goods or services or both redeemable against such token, voucher, coupon, or stamp.

12. It may be noted that Section 15(5) of the CGST Act provides that, the value of certain supplies as may be notified by the Government on the recommendations of the Council shall be determined in such manner as may be prescribed. Similarly Rule 32(7) provides that, the value of taxable services provided by such class of service providers as may be notified by the Government, on the recommendations of the Council, as referred to in paragraph 2 of Schedule I of the said Act between distinct persons as referred to in section 25 and where input tax credit is available, **shall be deemed to be** NIL. However, no such notifications have been issued.

    As per Rule 34(1) for the purposes of valuation, the rate of exchange for determination of value of taxable goods shall be the applicable rate of exchange as notified by the Board under section 14 of the Customs Act, 1962 for the date of time of supply of such goods in terms of section 12 of the Act.

13. **Reduction from value of supply in case of "Pure Agent"**

    In addition to above, there are also provisions dealing with value of supply of services in case of pure agent. As per section 15(2), the value of supply shall include incidental expenses, including commission and packing, charged by the supplier to the recipient of a supply and any amount charged for anything done by the supplier in respect of the supply of goods or services or both at the time of, or before delivery of goods or supply of services shall be included in the value of services. However, Rule 33 provides that, the expenditure or costs incurred by a supplier as a pure agent of the recipient of supply shall be excluded from the value of supply provided following conditions are met:

(i) the supplier acts as a pure agent of the recipient of the supply, when he makes the payment to the third party on authorisation by such recipient;

(ii) the payment made by the pure agent on behalf of the recipient of supply has been separately indicated in the invoice issued by the pure agent to the recipient of service; and

(iii) the supplies procured by the pure agent from the third party as a pure agent of the recipient of supply are in addition to the services he supplies on his own account

The term "pure agent" is defined as under:

(a) enters into a contractual agreement with the recipient of supply to act as his pure agent to incur expenditure or costs in the course of supply of goods or services or both;

(b) neither intends to hold nor holds any title to the goods or services or both so procured or supplied as pure agent of the recipient of supply;

(c) does not use for his own interest such goods or services so procured; and

(d) receives only the actual amount incurred to procure such goods or services in addition to the amount received for supply he provides on his own account

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CA Rajkamal Shah & CA Bharat Vasani

INDIRECT TAXES
GST – Legal Update

NOTIFICATIONS

Due date for filing of GSTR 1 & GSTR 3B extended in Odisha [Notification Nos. 23 & 24/2019-CGST dated 11-5-2019]

Registered persons whose principal place of business in the state of Odisha is at Angul, Balasore, Bhadrak, Cuttack, Dhenkanal, Ganjam, Jagatsinghpur, Jajpur, Kendrapara, Keonjhar, Khordha, Mayubhanj, Nayagarh or Puri; due date is extended as under:

Return Form	*Return Period*	*Extended Due Date*
GSTR 1 (monthly periodicity)	April' 2019	10-6-2019
GSTR 3B	April' 2019	20-6-2019

Extension of time limit for Real Estate developers to exercise option of lower tax rates [Notification No. 10/2019-CGST (Rate) dated 10-5-2019]

Time limit for real estate developers to exercise option to continue charging old rates (i.e. 12% or 18%) or opt for new rates (i.e. 1% or 5%) is extended from 10-5-2019 to 20-5-2019.

[Similar Notf. No. 9/2019 issued under IGST (Rate) and Notf. No. 10/2019 under UTGST (Rate) dated 10-05-2019]

Kerala flood cess levy is deferred to 1-7-2019

FAQ's – Real Estate [date 7th May, 2019 (part I) & 14th May, 2019 (part II)]

CBIC has released detailed FAQ's on real estate sector clarifying many doubts expressed by the industry with regards to new GST rate structure effective from 1-4-2019. The readers are requested to refer the Chamber's website.

Press release on clarifications re. : filing of Annual Return (GSTR-9)

The trade and industry have raised certain queries with respect to filing of this Annual return which are being clarified as follows:

a) Information contained in **FORM GSTR-2A** as on 1-5-2019 shall be auto-populated in Table 8A of **FORM GSTR-9.**

b) Input tax credit on inward supplies shall be declared from April 2018 to March 2019 in Table 8C of **FORM GSTR-9.**

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c) Particulars of the transactions for FY 2017-18 declared in returns between April 2018 to March 2019 shall be declared in Pt. V of **FORM GSTR-9**. Such particulars may contain details of amendments furnished in Table 10 and Table 11 of **FORM GSTR-1.**

d) It may be noted that irrespective of when the supply was declared in FORM **GSTR-1**, the principle of declaring a supply in Pt. II or Pt. V is essentially driven by when was tax paid through **FORM GSTR-3B** in respect of such supplies. If the tax on such supply was paid through **FORM GSTR-3B** between July 2017 to March 2018 then such supply shall be declared in Pt. II and if the tax was paid through **FORM GSTR-3B** between April 2018 to March 2019 then such supply shall be declared in Pt. V of **FORM GSTR-9.**

e) Any additional outward supply which was not declared by the registered person in **FORM GSTR-1** and **FORM GSTR-3B** shall be declared in Pt. II of the **FORM GSTR-9**. Such additional liability shall be computed in Pt. IV and the gap between the "tax payable" and "Paid through cash" column of **FORM GSTR-9** shall be paid through **FORM DRC-03.**

f) Many taxpayers have reported a mismatch between auto-populated data and the actual entry in their books of account or returns. One common challenge reported by taxpayer is in Table 4 of **FORM GSTR-9** where details may have been missed in **FORM GSTR-1** but tax was already paid in **FORM GSTR-3B** and therefore taxpayers see a mismatch between auto-populated data and data in **FORM GSTR-3B**. It may be noted that auto-population is a functionality provided to taxpayers for facilitation purposes, taxpayers shall report the data as per their books of account or returns filed during the financial year.

g) Many taxpayers have represented that Table 8 has no row to fill in credit of IGST paid at the time of import of goods but availed in the return of April 2018 to March 2019. Due to this, there are apprehensions that credit which was availed between April 2018 to March 2019 but not reported in the annual return may lapse. For this particular entry, taxpayers are advised to fill in their entire credit availed on import of goods from July 2017 to March 2019 in Table 6(E) of **FORM GSTR-9** itself.

h) Payments made through **FORM DRC-03** for any supplies relating to period between July 2017 to March 2018 will not be accounted for in **FORM GSTR-9** but shall be reported during reconciliation in **FORM GSTR-9C.**

Similarly press release is issued regarding clarifications on filing GSTR-9A. The readers are requested to refer the Chamber's website.

Further, Maharashtra Government has issued mechanism for redressal of difficulties faced by taxpayers due to technical glitches.

For space constraint the press release are not reproduced here and the readers are requested to refer the Chamber's website.

The Finance Ministry has clarified that, last date for filing of Annual return in FORM GSTR-9 will continue to be 30th June, 2019. The GSTN has updated the **GSTR-2A** till 31-5-2019. Therefore the taxpayers who had filed the return up to March 2019 is being auto-populated in **GSTR-2A** up to 31-5-2019.

Examination for GST Practitioner's [Press Release dated 1-5-2019 and Press Release cum Schedule dated 10-5-2019]

- Next exam for GST Practitioners' is scheduled on 14-6-2019 and 12-12-2019 from 11:00 am to 1:30 pm.

- The registration portal will be activated from 21-5-2019 to 4-6-2019 for those appearing on 14-6-2019.
- It may be noted that the exam to be held on 12-12-2019 is last exam to appear and pass.

TRADE CIRCULAR

Sub: **Mechanism for redressal of difficulties faced by taxpayers due to technical glitches on the portal www.mahagst.gov.in. of the Maharashtra Goods and Services Tax Department**

No:– JC-MAHAVIKAS/GST/MGSTD_IT_ Grievance Redressal/B-2235, dated 1-6-2019

Trade Circular No. 38T of 2019

Background and scope

1. Department of **Goods and Services Tax**, Maharashtra has made available various services in phased manners for making on line compliance in respect of various provisions related to Registration, Returns, Payments, e-CST declaration, refunds, Form 704 etc. Some other functionalities are likely to be made available to users very soon.

2. During course of implementation, it is observed that some taxpayers are facing difficulties while making transaction on the departmental MAHAGST portal www.mahagst.gov.in. The difficulties faced by taxpayers are either functional (i.e., due to lack of understanding on operational procedures) or technical i.e., due to technical hitches on portal or in applications of automation system.

3. On departmental MAHAGST portal, department has already made available facility to create service tickets and taxpayers are expected to create service tickets in respect of such difficulties faced while carrying out transaction on the MAHAGST Portal.

4. The department has also established central inbound helpdesk having toll free number **1800 225 900**, wherein taxpayers can raise the difficulties faced by him. In addition, department has set up helpsdesks at various location to provide immediate support to difficulties faced by taxpayers, however these departmental helpdesk are able to resolve functional difficulties. The technical difficulties due to hitches on the MAHAGST Portal are referred to on technical team of department.

5. It is observed that in some of the cases technical difficulties faced by taxpayers are not resolved before time prescribed for compliance under various provisions of different [a]cts administered by department. This resulted in non-compliances or delayed compliance by taxpayers, making them liable for penal actions for such non compliances.

6. In such cases taxpayers have been requesting various departmental authorities to grant concessions/waivers from actions for non-compliance or delayed compliances which are attributed to technical glitches of automation system.

7. In order to take decision on such request for concessions/waivers from actions, IT —Grievance Redressal Mechanism is set up in the department

8. **Mechanism for redressal**

   Taxpayers, who could not make electronic compliance under various provisions of different Acts due to technical glitches of departmental portal wvvw.mahagst.gov.in and making them liable for penal actions for such non compliance or delayed compliances under various provisions of Act can make an application for redressal under this mechanism.

   A. In order to get resolution through this mechanism, a taxpayer shall,

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a. create service ticket through service request functionality available on the departmental portal www.mahagst.gov.in.

b. make an application to his nodal officer in format prescribed as Annexure A through. Physical application or by mail to the nodal officer. The information of nodal officer of taxpayers is available on the www,mahagstgov.in.

c. file separate application for grievances in respect of individual issue. While filing an application taxpayer shall mention the name of function/module along with the nature of difficulties at the appropriate place provided in an application. The names of functions/modules are given in the Annexure B.

B. The said application shall be accompanied by necessary evidences to establish that a *bona fide* attempt, to comply with the due process of law, was made by the taxpayer. The evidences may include either

i. Service Ticket number created on the Mahagst portal on or before due date, or

ii. screen-shots of the system taken on-or before due date, or

iii. Correspondence made with departmental authorities if any on or before due date, or

iv. Any other information/ document, which shows that an attempt has been made.

C. The Nodal Officer will verify the application and the evidence submitted by taxpayers and forward observations/ recommendations in **prescribed format** to the appropriate authority as may be declared for IT redressal.

D. The taxpayer having any grievances in respect of the application for redressal made to nodal officer may apply to respective locational or Divisional Supervisory authority.

However, facility under this mechanism shall not be available to the cases where non-compliances are due to the reasons other than technical glitches like non-availability of internet to the dealer, problem of individual taxpayer or any other localised problem. If the issue/problem is due to some legal/procedural reason the same is not come into ambit of MAHAIT Grievance Redressal Mechanism.

ANNEXURE-A

Application for Redressal of difficulties faced due to technical glitches on portal www.mahagst.gov.in. of the Maharashtra Goods and Services Tax Department

Sr. No.	*Particulars*	*Details*
1	Registration number – TIN	
2	Legal name of the Taxpayer	
3	E-mail of the authorised signatory for communication	

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Sr. No.	Particulars		Details
4	Phone no of the authorized signatory for communication		
5	Axt (Refer Annexure C of Trade Circular)		
6	Category of the Functionality/Module (Refer Annexure B of Trade Circular)		
7	Description of issue/problem in detail		dd/mm/yyyy
8	When did the taxpayer first attempt to file?		
9	Nature of error noticed in first filing (attach screen shots and other evidences like emails sent)		
10	Details of subsequent attempts of filing (chronologically) (enclose evidences)		
11	Nature of the errors/message received while attempting to file subsequently (attach screen shots and other evidences)		
12	Details of communication of the problem to the helpdesk		
	a.	Date of communication	
	b.	Service Request/ticket numbers.	
	c.	Whether communication received from helpdesk (If yes provide evidence in support of the same)	Yes/No

Place:
Date :

Name and Signature of authorized signatory

Annexure B
Names of Modules/Functions

Sr. No.	*Function/Module*
1	Registration
2	Returns
3	Payments
4	Refund
5	Assessment and Audit
6	Recovery
7	Appeals
8	Form 704
9	Legal/MSTT
10	E-CST Declarations
11	Website — Portal
12	Mobile applications
13	MIS Reports
14	Profession Tax
15	Chit Fund
16	Help Desk, Grievances, Complaints, RTI
17	e-WAY Bill
18	Others

Annexure C
Names of Acts

Sr. No.	*Function/Module*	*Head*
1	Maharashtra Value Added Tax	MVAT
2	Central Sales Tax Act	CST
3	Profession Tax Registration	PTRC
4	Profession Tax Enrollment	PTEC

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F. No. 354/32/2019-TRU
Government of India Ministry of Finance Department of Revenue (Tax Research Unit)
Dated the 14th May, 2019, New Delhi

Subject: FAQs (Part II) on real estate- reg.
A number of issues have been raised regarding the new GST rate structure notified for real estate sector effective from 01-04-2019. A compilation of Frequently Asked Questions (FAQs) containing 41 questions was issued on 7th May, 2019. Part II of the FAQ is presented below. The answers to the FAQs have been given in simple language for guidance and easy understanding of all stakeholders in the real estate sector. They do not have force of law. In case of conflict, the gazette notifications, which have legal force, shall have precedence.

Sl. No.	*Question*	*Answer*
1.	In case of an area sharing arrangement between a Landowner-Promoter and a Developer-Promoter, where the Project qualifies to be considered an "Ongoing Project", whether an option of 1% or 5% (without ITC) *vis-à-vis* 8% or 12% (with ITC) as prescribed in Notification No. 3/2019 can be exercised by the Developer-Promoter and Landowner-Promoter independently?	The legal and operational harmony necessitates that both the Landowner-Promoter and the Developer-Promoter exercise identical option for a project.
2.	In case of an area sharing arrangement between a Landowner-Promoter and a Developer-Promoter in a New Project undertaken on or after 1/4/2019, whether the new rate of 1% or 5% is applicable in case of the Landowner-Promoter who sells the under-construction premises before completion of the project? Will the Landowner-Promoter be entitled to ITC in respect of tax charged to him by the Developer-Promoter on such supply? Whether the Landowner-Promoter shall be entitled/to avail ITC on any other services or goods used by him in furtherance of his business (such as brokerage on sales etc.)?	The new effective rates of 1% and 5% without ITC are applicable to the apartments booked by the Land owner-promoter in an ongoing project as well as a new project which commences on or after 1-4-2019. The Landowner Promoter shall be entitled to ITC in respect of tax charged to him by the Developer Promoter on construction of such apartments. However, the Landowner Promoter shall not be entitled to avail ITC on any other services or goods used by him.
3.	Residential Real Estate Project (RREP) shall mean a REP in which the carpet area of the commercial apartments is not more than 15% of the total carpet area of all the apartments in the REP (Clause xix). "Carpet area" shall have the same meaning as assigned to it in	The term "Residential Real Estate Project (RREP) has been defined in the notification to mean a REP in which the carpet area of the commercial apartments is not more than 15 per cent of the total carpet area of all the apartments in the REP.

Sl. No.	*Question*	*Answer*
	clause (k) of Section 2 of the RERA, 2016. Whether non-saleable areas such as society office, club house, etc., are to be taken into consideration for determining 15% for deciding whether the project is RREP or not?	Apartments shall be taken as commercial or residential apartments as declared to RERA authority.
4.	For the purpose of determining the threshold of ₹ 45 lakh in case of "affordable residential apartment", whether the following charges generally recovered by the developer from the buyer shall be included? • Amenity Charges • Society formation charges • Advance maintenance • Legal Charges	For the purpose of determining the threshold of the gross amount of ₹ 45.00 lakh for affordable residential apartments, all the charges or amounts charged by the promoter from the buyer of the apartments shall form part of the gross amount charged. Clause xvi, sub-clause (a)(ii)(C) of paragraph 4 of notification No. 11/2017-CT(R) dated 28-6-2017, reproduced below, refers. *"C. Any other amount charged by the promoter from the buyer of the apartment including preferential location charges, development charges, parking charges, common facility charges etc."* However the value shall not include stamp duty payable/to/the/statutory/ authority/maintenance charges/deposits for maintenance of apartment or maintenance of common infrastructure.
5.	In case of a Real Estate Project, comprising of Residential as well as Commercial portion (more than 15%), how is the minimum procurement limit of 80% to be tested, evaluated and complied with where the Project has single RERA Registration and a single GST Registration and it is not practically feasible to get separate registrations due to peculiar nature of building(s)?	The promoter shall apportion and account for the procurements for residential and commercial portion on the basis of the ratio of the carpet area of the residential and commercial apartments in the project.
6.	In an area sharing model, a promoter has to handover constructed flats/apartments to the land owner who supplied TDR for the project. Value of TDR at the time when the landowner transferred it to the promoter is not known. How would the promoter determine GST on TDR?	Value of TDR, shall be equal to the amount charged by the promoter for similar apartments from the independent buyers booked on the date that is nearest to the date on which such development rights or FSI is transferred by the land owner to the promoter.

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Sl. No.	*Question*	*Answer*
7.	In the formula prescribed under first proviso to Entry 41A of the Notification 12/2017-CT (R), as amended by Notification 4/2019-CT (R), what rate shall be taken to determine the value to be ascribed to the "GST Payable on TDR or FSI or both for construction of the residential apartments in the project but for exemption contained therein" as no specific rate has been prescribed in Notification 11/2017-CT-Rate or any other notification? What is the rate applicable to output supply of TDR or FSI? Whether the quantum of TDR or FSI (including additional FSI) or both shall be taken only in respect of un-booked apartments as on the date of issuance of Completion Certificate or first occupation of the project for the purpose of formula?	The GST on transfer of development rights or FSI (including additional FSI) is payable at the rate of 18% (9% + 9%) with ITC under Sl. No. 16, item (iii) of Notification No. 11/2017-Central Tax (Rate) dated 28-6-2017 (heading 9972). There is no exemption on TDR or FSI (Addl. FSI) for construction of commercial apartments. Therefore, GST shall be payable on TDR or FSI (including additional FSI) or both used in respect of (i) carpet area of commercial apartment and (ii) unbooked residential apartments as on the date of issuance of Completion Certificate or first occupation of the project for the purpose of formula.
8.	In case of Redevelopment, Slum Rehabilitation or similar arrangements, the Developer will be constructing two types/ of units i.e., one which is allotted to existing occupiers for no monetary consideration and second which is sold in the market to outside buyer. Price at which the unit is being sold to the outsider is determined in a manner to factor cost of construction of both type of units so that the unit to existing occupiers may be allotted free of monetary consideration. It may be clarified whether the Input Tax Credit in relation to construction of units to be allotted to existing occupiers, in case of residential project opted for old rates or commercial projects, shall be allowed to the Developer.	The apartments given to the original inhabitants or the slum dwellers in redevelopment project or slum rehabilitation project are given by the promoter against consideration received by them in the form of TDR/FSI/monetary consideration from the original inhabitants in case of redevelopment projects and from the Government in case of slum rehabilitation projects. The supply of service by way of construction of such apartments against construction wholly or partly in the form of TDR/FSI is a taxable supply subject to GST. Wherever tax is paid on construction of such apartments at the effective rates of GST of 8%/12% with ITC, the promoters shall be eligible for ITC, including ITC in relation to construction of units to be allotted to the existing occupiers even though there may not be a monetary consideration but the consideration is in the form of grant of TDR/ FSI.

Sl. No.	*Question*	*Answer*
9.	In case of redevelopment or slum rehabilitation project, (new or an existing project) whether the constructed units supplied to existing occupiers by the developer free of monetary consideration are taxable? In case of ongoing project in respect of which the promoter has opted for new rates of 1%/5%, it may be clarified whether the units being supplied free of monetary consideration to existing dwellers will fall within the definition of affordable housing when certain units being sold in the open market are eligible for concessional rates under the category of Credit Linked Subsidy Scheme i.e., sub-item (da) of item (iv) of Sl. No. 3 of notification No. 11/2017-CTR?	Yes, units supplied free of cost also attract GST as their consideration is not money but TDR/FSI or rights relatable to land on which construction takes place. In such an ongoing project, the units sold in open market would be eligible for GST rate of 1% (without ITC), if such units are covered under Credit Linked Subsidy Scheme, as provided in the definition of "affordable residential apartments" given in notification no. 11/2017-CTR dated 28-6-2017 as amended by notification No. 3/2019-CTR dated 29-3-2019. The apartments being constructed in such ongoing project, for existing slum dwellers/occupiers shall be eligible for 1% rate if they meet the definition of affordable residential apartment, as under- (a) They have carpet area of less than 60 sqm. in specified metropolitan cities or 90 sqm. in places other than the specified metropolitan cities and the gross amount charged for similar apartments from independent buyers is not more than rupees 45 lakh. (Please refer to para 2A of notification No. 11/2017- CTR dated 28-6-2019 as amended *vide* notification No. 3/2019-CTR dated 29-3-2019), or (b) They are being constructed under any of the schemes specified in sub-item (b), sub-item (c), sub-item (d), sub-item (da) and sub-item (db) of item (iv); sub-item (b), sub-item (c), sub-item (d) and sub item (da) of item (v); and sub-item (c) of item (vi), against serial number 3 of the said notification.
10.	What shall be the rate of GST applicable on projects in respect of which OC has been issued prior to 1-4-2019, but the balance demands are pending? Such projects are neither projects which commence on or after 1-4-2019 nor ongoing projects.	Time of supply of the service by way of construction of apartments in such projects falls prior to 1-4-2019 and accordingly the rates as existed prior to 1-4-2019 would apply to such balance demands.

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Sl. No.	*Question*	*Answer*
11.	The affordable residential apartment should not have a carpet area exceeding 60 sqm in metropolitan cities and 90 sqm in other places. Will the internal walls of the apartment, balcony or verandah be included 60/90 sq. meter?	"Carpet area" is defined in clause (k) of section 2 of the RERA, 2016 and the same has been adopted in the notification.
12.	If an unregistered person transfers development right to a developer-promoter, then it is apparently not covered by the fourth//proviso//applicable//to clause (i) to clause (id) of serial 3 of Notification No. 11/2017 (as amended). Will the promoter be liable to pay GST on TDR received from an unregistered land owner?	Promoter shall be liable to pay GST on TDR transferred by any person whether registered or not on RCM basis.
13.	Whether the ITC availed as per the second proviso applicable to clause (i) to clause (id) of serial 3 of Notification No. 11/2017 (as amended) can/be/adjusted against the output liability of 5%/1%?	No. GST on services of construction of an apartment by a promoter at the rate of 1%/5% is to be discharged in cash only. ITC, if any, may be used for discharging any other supply of service.
14.	If a Developer-Promoter opts to pay tax for the ongoing project of affordable residential apartment at the new rate, can he use the ITC available to him under the second proviso applicable to clause (i) to clause (id) of serial 3 of Notification No. 11/2017 (as amended) for payment of tax at 1%/5%?	Reply as in Q. No. 13 above.
15.	The condition in Notification No. 3/2019 specifies that 80% of inputs and input services should be procured from registered person. What about expenditure such as salaries, wages, etc., These are not supplies under GST [Sl. 1 of Schedule III]. Now, my question is, whether such services will be included under input services for considering 80% criteria?	Services by an employee to the employer in the course of or in relation to his employment are neither a goods nor a service as per clause 1 of the Schedule III of CGST Act, 2017. Therefore, salaries and wages paid by promoter to his employees will not be relevant for the minimum purchase requirement of 80%.
16.	A buyer has booked an apartment prior to 1st April, 2019 and paid part consideration to the developer. The developer decides to opt for the new scheme for this ongoing project. Will the buyer be required to pay any additional tax for such payment he has made prior to 31st March, 2019?	No. For the past payments made before the transition date (1-4-2019), no additional GST is required to be paid.

Sl. No.	*Question*	*Answer*
17.	Whether the condition of receiving 80% of inputs/and input services from the registered person shall be applicable if the developer opts to continue to pay tax at the old rates of 12%/8% in respect of an ongoing project?	No, if the developer opts to continue to pay tax at the old rates of 12%/8% in respect of an ongoing project, the condition of receiving 80% of inputs and input services from the registered person doesn't apply.
18.	Whether the inward supplies of exempted goods/services shall be included in the value of supplies from unregistered persons while calculating 80% threshold?	Yes. Inward supplies of exempted goods/services shall be included in the value of supplies from unregistered persons while calculating 80% threshold.
19.	Whether the purchase of Land from an unregistered person shall be required to be included in the value of Input and Input Services for the purpose of calculation of 80% threshold?	No. As per Schedule III, Entry No 5, of CGST Act, sale of land is not a supply. In addition, as per 5th proviso to entries at Sl. No. (i), (ia), (ib), (ic) and (id) against Serial No 3 in the Notification No.11/2017-CTR dated 28-6-2017 as amended by Notification No. 3/2019-CTR dated 30-3-2019, transactions by way of grant of development rights, long term lease, FSI etc. are not required to be included in the value of Input and Input Services for evaluation of criteria/of 80% from registered persons.
20.	When a developer prefers the option of paying tax at 1%/5%, without ITC, for an ongoing project, whether the apartments which were not considered as affordable in the earlier scheme (though certain apartments in such project were considered as affordable in the earlier scheme) will be considered as affordable after 1st April, 2019, if such apartments fit the definition of affordable residential apartments as provided in notification No. 3/2019-CT(R) dated 29-3-2019?	Yes, in case of an ongoing project in respect of which the promoter has not opted to pay GST at the old rate, he shall pay tax at the effective rate of 1% without ITC on apartments which meet the new definition of affordable residential apartment.
21.	Whether the amended Rule 42 shall apply to all RREPs including ongoing projects?	In case of an ongoing RREP, in respect of which promoter opts for the new rates of 1%/5% and which underwent transition of ITC consequent to change of rates of tax on 1-4-2019, ITC determined under sub-rule (1) of Rule 42 shall not be required to be calculated finally on the completion or first occupation of the RREP.

Sl. No.	*Question*	*Answer*
22.	Whether separate Form (Annexure IV) shall be filed by the Developer in respect of each of the Ongoing Projects?	Yes. The promoter has to exercise the option for payment of tax at the old rates of 8%/12% with ITC for each of the ongoing projects separately.
23.	On what basis a Contractor/Sub-contractor executing a composite supply of works contract in terms of clause (va) i.e., 12% for affordable residential apartments, shall satisfy himself as regards condition of 50% of the total carpet area?	The contractor may charge tax on the works contract service provided by him to a promoter at the concessional rate of 12% under/notification No./11/2017-CTR/ dated 28-6-2019,/S./No. 3, entry (va) on the basis of a declaration by the promoter to the contractor that the project meets the conditions prescribed for concessional rate of GST on works contract service prescribed under the said entry.
24.	Whether the condition to make payment within 180 days/by Land Owner-Promoter to Developer-Promoter as provided in second proviso to section 16(2), shall be applicable for reversal of input tax credit?	The apartments given to the Landowner-Promoter are given by the Developer-Promoter against consideration received by him in the form of TDR from the Landowner-promoter. Therefore, the payment by Landowner-Promoter for service of construction of apartments received from the Developer-Promoter is made even before the service is provided. Therefore, Landowner-Promoter shall not be required to reverse input tax credit of tax charged from him by the Developer-Promoter on the ground that he has not made payment for the service received/from the Developer-Promoter.
25.	Whether the exemption given by way of Entry 41A/41B of Notification No. 12/2017-CTR shall be available in respect of development rights etc., transferred to a person other than promoter? Please clarify whether sub-clause (v) in clause (zk) in section 2 in RERA Act, 2016 covers a person who purchases TDR as developer?	The exemption is available only on TDR/ FSI transferred on or after 1st April, 2019 for construction of residential apartments by a promoter in a real estate project.
26.	How to determine value of construction services/provided by the promoter to land owner in lieu of transfer of development rights, when land owner is not registered?	Value of construction services provided by the promoter to land owner in such cases shall be determined based on the total amount charged by the promoter for similar apartments in the project from independent buyers, other than the land owner, nearest to the date on which such development right

Sl. No.	*Question*	*Answer*
		etc. is transferred to the promoter, less the value of transfer of land, if any, as prescribed in paragraph 2 of Notification No. 11/2017-CT(R) dated 28-6-2017.
27.	In case of a project, where completion certificate has been received prior to 31-3-2019 but some part of the consideration in relation to the apartment is due after 31-3-2019, it appears that such project will not qualify as ongoing project. What will be the applicable tax rate on such amount received on or after 1-4.2019 – old rate or new rate?	Time of supply of service of construction of such apartments is prior to 1-4-2019 and the same shall be subject to tax at the old rates of 12%/8%.

F. No. 354/32/2019-TRU
Government of India Ministry of Finance Department of Revenue (Tax Research Unit)
dated the 7th May, 2019, New Delhi

Subject: FAQs on real estate- reg.

A number of issues have been raised regarding the new GST rate structure notified for real estate sector effective from 1-4-2019. A compilation of Frequently Asked Questions (FAQs) is presented below. The answers to the FAQs have been given in simple language for guidance and easy understanding of all stakeholders in the real estate sector. They do not have force of law. In case of conflict, the gazette notifications, which have legal force, shall have precedence.

<table>
<tr><th>Sr. No.</th><th>Question</th><th>Answer</th></tr>
<tr><td>1.</td><td>What are the rates of GST applicable on construction of residential apartments?</td><td>With effect from 1-4-2019, effective rate of GST applicable on construction of residential apartments by promoters in a real estate project are as under:
<table>
<tr><th>Description</th><th>Effective rate of GST (after deduction of value of land)</th></tr>
<tr><td>Construction of affordable residential apartments</td><td>1% without ITC on total consideration.</td></tr>
<tr><td>Construction of residential apartments other than affordable residential apartments</td><td>5% without ITC on total consideration.</td></tr>
</table>
</td></tr>
</table>

Sr. No.	*Question*	*Answer*
		The above rates are effective from 1-4-2019 and are applicable to construction of residential apartments in a project which commences on or after 1-4-2019 as well as in ongoing projects. However, in case of ongoing project, the promoter has an option to pay GST at the old rates, i.e. at the effective rate of 8% on affordable residential apartments and effective rate of 12% on other than affordable residential apartments and, consequently, to avail permissible credit of inputs taxes; in such cases the promoter is also expected to pass the benefit of the credit availed by him to the buyers.
2.	What is an affordable residential apartment?	Affordable residential apartment is a residential apartment in a project which commences on or after 1-4-2019, or in an ongoing project in respect of which the promoter has opted for new rate of 1% (effective from 1-4-2019) having carpet area up to 60 square meters in metropolitan cities and 90 square meters in cities or towns other than metropolitan cities and the gross amount charged for which, by the builder is not more than forty five lakh rupees. [Cities or towns in the notification shall include all areas other than metropolitan city as defined, such as villages.] In an ongoing project in respect of which the promoter has opted for new rates, the term also includes apartments being constructed under the specified housing schemes of Central or State Governments. [Metropolitan cities are Bengaluru, Chennai, Delhi NCR (limited to Delhi, Noida, Greater Noida, Ghaziabad, Gurgaon, Faridabad), Hyderabad, Kolkata and Mumbai (whole of MMR) with their geographical limits prescribed by Government.]
3.	What is an ongoing project?	A project which meets the following conditions shall be considered as an ongoing project.

Sr. No.	*Question*	*Answer*
		(a) Commencement certificate for the project, where required, has been issued by the competent authority on or before 31st March, 2019, and it is certified by a registered architect, chartered engineer or a licensed surveyor that construction of the project has started (i.e., earthwork for site preparation for the project has been completed and excavation for foundation has started) on or before 31st March, 2019. (b) Where commencement certificate in respect of the project, is not required to be issued by the competent authority, it is to be certified by any of the authorities specified in (a) above that construction of the project has started on or before the 31st March, 2019. (c) Completion certificate has not been issued or first occupation of the project has not taken place on or before the 31st March, 2019. (d) Apartments of the project have been, partly or wholly, booked on or before 31st March, 2019.
4.	Does a promoter or a builder here option to pay tax at old rates of 8% & 12% with ITC?	Yes, but such an option is available in the case of an ongoing project. In case of such a project, the promoter or builder has option to pay GST at old effectivrate of 8% and 12% with ITC. To continue with the old rates, the promoter/builder has to exercise one time option in the prescribed form and submit the same manually to the jurisdictional Commissioner by the 10th of May, 2019. However, in case where a promoter or builder does not exercise option in the prescribed form, it shall be deemed that he has opted for new rates in respect of ongoing projects and accordingly new rate of GST i.e., 5%/1% shall be applicable and all the provisions of new scheme including transitional provisions shall be applied.

<table>
<tr><th>Sr. No.</th><th>Question</th><th>Answer</th></tr>
<tr><td></td><td></td><td>There is no such option available in case of projects which commence on or after 1-4-2019. Construction of residential apartments in projects commencing on or after 1-4-2019 shall compulsorily attract new rate of GST @ 1% or 5% without ITC.</td></tr>
<tr><td>5.</td><td>What is the rate of GST applicable on construction of commercial apartments [shops, godowns, offices etc.] in a real estate project?</td><td>With effect from 1-4-2019, effective rate of GST, after deduction of value of land or undivided share of land, on construction of commercial apartments [shops, godowns, offices etc.] by promoter in real estate project are as under:
<table>
<tr><td>Description</td><td>Effective rate of GST (after deduction of value of land)</td></tr>
<tr><td>Construction of a Residential Real Estate Project (RREP), as explained in question no. 6 below, which commences on or after 1-4-2019 or in an ongoing project in respect of which the promoter has opted for new rates effective from 1-4-2019</td><td>5% without ITC on commercial apartments total consideration</td></tr>
<tr><td>Construction of a Real Estate Project (REP) other than Residential Real Estate Project (RREP) or in an ongoing project in respect of which the promoter has opted for old rates</td><td>12% with ITC on total commercial apartments consideration</td></tr>
</table></td></tr>
<tr><td>6.</td><td>What is a Residential Real Estate Project?</td><td>A “Residential Real Estate Project” means a “Real Estate Project” in which the carpet area of the commercial apartments is not more</td></tr>
</table>

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Sr. No.	*Question*	*Answer*
		than 15 per cent of the total carpet area of all the apartments in the project.
7.	What is the criteria to be used by an architect, a chartered engineer or a licensed surveyor for certifying that construction of the project has started by 31st March, 2019	Construction of a project shall be considered to have been started on or before 31st March, 2019, if the earthwork for site preparation for the project has been completed, and excavation for foundation has started on or before the 31st March, 2019.
8.	Does a promoter/builder have to purchase all goods and services from registered suppliers only?	A promoter shall purchase at least eighty per cent of the value of input and input services, from registered suppliers. For calculating this threshold, the value of services by way of grant of development rights, long term lease of land, floor space index, or the value of electricity, high speed diesel, motor spirit and natural gas used in construction of residential apartments in a project shall be excluded.
9.	If value of purchases as prescribed above from registered supplier is less than 80%, what would be the applicable GST rate on such purchases?	Promoter has to pay GST @ 18% on reverse charge basis on all such inward supplies (to the extent short of 80% of inward supplies from registered supplier) except cement on which tax has to be paid (by the promoter on reverse charge basis) at the applicable rate, which at present is 28% (CGST 14% + SGST 14%).
10.	In case of new rate of 5%/1%, whether the conditions of payment of tax through Cash Ledger, payment of tax under RCM subject to 80% limit, non-availing of Input Tax Credit, reversal of credit, maintenance of project wise account, reporting of ITC not availed in corresponding GSTR-3B etc. are required to be complied mandatorily by the Developer?	Yes. All the specified conditions against clause (i) to (id) of Sl. No. 3 of Notification No. 11/2017- CTR are mandatory.
11.	What is the rate of GST applicable on transfer of development rights, FSI and long term lease of land?	Supply of TDR or FSI or long term lease of land used for the construction of residential apartments in a project that are booked before issue of completion certificate or first occupation is exempt. Supply of TDR or FSI or long term lease of land, on such value which is proportionate to construction of residential apartments

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Sr. No.	Question	Answer
		that remain unbooked on the date of issue of completion certificate or first occupation, would attract GST at the rate of 18%, but the amount of tax shall be limited to 1% or 5% of value of apartment depending upon whether the residential apartments for which such TDR or FSI is used, in the affordable residential apartment category or in other than affordable residential apartment. TDR or FSI or long term lease of land used for construction of commercial apartments shall attract GST of 18%. The above shall be applicable to supply of TDR or FSI or long term lease of land used in the new projects where new rate of 1% or 5% is applicable.
12.	Who is liable to pay GST on TDR and floor space index?	The promoter is liable to pay GST on TDR or floor space index supplied on or after 1-4-2019 on reverse charge basis.
13.	At what point of time, the promoter should discharge its tax liability on TDR?	The liability to pay GST on development rights shall arise on the date of completion or first occupation of the project, whichever is earlier. Therefore, promoter shall be liable to pay tax on reverse charge basis, on supply of TDR on or after 1-4-2019, which is attributable to the residential apartments that remain unbooked on the date of issuance of completion certificate, or first occupation of the project.
14.	At what point of time, the promoter should discharge its tax liability on FSI (including additional FSI)?	On FSI received on or after 1-4-2019, the promoter should discharge his tax liability on FSI as under: (i) In case of supply of FSI wherein consideration is in form of construction of commercial or residential apartments, liability to pay tax shall arise on date of issuance of Completion Certificate. (ii) In case of supply of FSI wherein monetary consideration is paid by promoter, liability to pay tax shall arise on date of issuance of Completion Certificate only if such FSI is relatable to

Sr. No.	*Question*	*Answer*
		construction of residential apartments. However, liability to pay tax shall arise immediately if such FSI is relatable to construction of commercial apartments.
15.	At what point of time, the promoter should discharge its tax liability on supply of long term lease?	On long term lease received on or after 1-4-2019, the promoter should discharge his tax liability on long term lease as under: In case of supply of long term lease of land for construction of commercial apartments, tax shall be paid by the promoter immediately. However, for construction of residential apartment, liability to pay tax on the upfront amount payable for long term lease shall arise on the date of issuance of Completion Certificate.
16.	Land Development Corporation of Orissa has provided land on long term lease for 99 years, for construction of a real estate project. As per the lease agreement, promoter has to pay an upfront amount of ₹ 10 crore and annual/monthly licence fee of ₹ 5 lakh. Does the promoter have to pay GST on these amounts?	The liability to pay tax on Long term lease of land (30 years or more) received against consideration in the form of upfront amount and periodic licence fee is on the promoter. The promoter has to discharge tax liability on the same on RCM basis. However, the upfront amount payable for the long term lease (known as premium, salami, cost, price, development charges etc.) is exempt to the extent it is used for construction of residential apartments that are booked before issuance of completion certificate or first occupation. Annual/monthly rent or licence fee payable for long term lease is taxable under GST.
17.	Someone booked a flat from XYZ Developers in June, 2018. As of 31-3-2019, he had paid 40% of the value of the flat. What shall be the GST rate applicable on the remaining portion of value of the flat?	GST on the remaining portion of the value of flat payable to the promoter on or after 1-4-2019 as per the contract between the promoter and buyer shall be payable at effective rate of 1% or 5%, subject to the condition that the builder has not exercised the option to pay tax on construction of apartments at the old rates of 12% or 18%. If the XYZ developer exercises option to continue to pay tax at old effective rate of 8% or 12% by 10th May, 2019, then GST has to be paid @ 8% or 12% on remaining portion

Sr. No.	*Question*	*Answer*
		of the value of the flat; in such cases, the promoter would be entitled to permissible credit of input taxes and, as such, the price that he charges from the buyer should appropriately reflect this credit.
18.	I am a beneficiary of PMAY- CLSS and carpet area of my house being constructed in an ongoing project is 150 sq m. Am I eligible for new rate of 1% on same?	You are eligible for new GST rate of 1%, subject to the condition that the developer-promoter with whom you have booked the house has not exercised option to pay tax on construction of apartments at the old rate of 8%.
19.	I am planning to purchase an apartment in a newly launched project. The project has been launched after 31-3-2019 by XYZ Developers at Noida. Price of the apartment having carpet area of 80 sqm is ₹ 48 lakhs. What is the rate of GST applicable on construction of this apartment?	The tax rate applicable on construction of the apartments in a project that commences on or after 1-4-2019 would be 5%.
20.	I have already paid tax of 12% (effective) on instalments paid before 1-4-2019. I wish to get the benefit of new rate of 1% or 5%. Whether it is the builder or the buyer who has the option to pay tax at the new or old rates?	The buyer cannot exercise option to pay tax at the new or old rates. It is the builder,who has to exercise the option to pay tax on construction of apartments at the old rate of 12% latest by 10th May, 2019. If the builder doesn't exercise his option to continue to pay tax at the old rate by the said date, then the effective GST rate applicable on all your instalments payable to the builder on or after 1-4-2019 as per the contract shall be either 1% or 5%, depending on whether the apartment is an affordable or other than affordable residential apartment.
21.	In respect of supply made in an ongoing Project covered by clauses (ie) and (if) of Entry 3 of Notification No. 3/2019, CT (R), an option is required to be exercised by the Promoter in Annexure IV by 10th May, 2019. At the same time, it is permissible for him to issue invoices between 1st April, 2019 to 9th May, 2019 which shall, however, be in conformity with the option to be exercised. Whether it is permissible for the Promoter to revise the invoice as provided in	Where the GST rate at which tax has been charged in the invoices issued by the promoter prior to 10th May, 2019 are not in accordance with the option required to be exercised by him on or before 10th May, 2019 to pay GST on construction of apartments in an ongoing project at either the new or old rates, the promoter may issue debit or credit notes in accordance with Section 34 of CGST Act, 2017.

Sr. No.	*Question*	*Answer*
	Section 34 of CGST Act, 2017, including by way of issuance of Credit/Debit Notes so as to bring the transaction in conformity with the option exercised by the Promoter ultimately by 10th May, 2019?	
22.	How to compute adjustment of tax in a Credit Note to be issued u/s. 34 by Real Estate Developer in case unit was booked prior to 1st April, 2019 on which GST was paid on part consideration received at the time of booking, but cancelled after 1st April, 2019.	Developer shall be able to issue a Credit Note to the buyer as per provisions of section 34 in case of change in price or cancellation of booking provided that the amount received in excess if any, consequent to issuance of Credit Note, is refunded to the Buyer by the Developer before September following the end of the financial year. Developer shall be able to take adjustment of tax paid in respect of the amount of such Credit Note. For example, a Developer who paid GST of ₹ 1,20,000 at the rate of 12% (effectively) in respect of a gross amount of booking of ₹ 10,00,000 before 1st April, 2019 shall be entitled to take adjustment of tax of ₹ 1,20,000 upon cancellation of the said booking on or after 1st April, 2019 against other liability of GST including liability arising at the rate of 5%/1% provided that the entire amount received from the buyer is refunded by the Developer. Further, in case apartments booked prior to 1-4-2019 on which GST has been paid till 31-3-2019 at the old rates of 8%/12% with ITC, are cancelled and rebooked at the new rates of 1%/5% without ITC or sold after issuance of completion certificate, the credit taken in respect of such apartments for supply of service till 31-3-2019 on which tax was paid @ 8%/12% with ITC shall be required to be reversed.
23.	Whether the option to pay tax at the applicable effective rate of 12% or 8% (with ITC) is available to the Promoter in respect of the New Project, which has been commenced on or after 1st April, 2019?	No, there is no option to pay tax at the effective rate of 12% or 8% with ITC on construction of residential apartments in projects which commences on or after 1-4-2019.

Sr. No.	*Question*	*Answer*
24.	From the plain reading of the provisions and the definitions of the various terms as defined in the Notification No. 3/2019-CT(R), it appears that the one-time option is required to be exercised for the entire REP or RREP. Does this mean that a promoter can opt for old rates or new rates, as the case may be, for different projects being undertaken by him under the same entity?	Yes. The option to pay tax on construction of apartments in the ongoing projects at the effective old rates of 8% and 12% with ITC has to be exercised for each ongoing project separately. As per RERA, 2016, project wise registration is allowed. So, the promoter may exercise different options for different ongoing projects being undertaken by him.
25.	In respect of the construction and supply of premises under specific schemes like PMAY, Housing for All (Urban), RAY etc. as mentioned in sub items (b), (c), (d), (da), (db) of item (iv) and sub-items (c), (d), (da) of item (v) of Entry 3 of Notification 11/2017 – CT (R), whether the pre-existing effective rate of 8%, with ITC benefit continues to be available in case of any New Project that has commenced under any such scheme after 1-4-2019?	No. The rate of 8% and 12% with ITC is not available for construction of apartments in a project that commences on or after 1-4-2019. It makes no difference whether or not the apartments are being constructed under PMAY or any other housing schemes of the Central or State Government.
26.	In respect of any ongoing project undertaken under the specific schemes like PMAY, Housing for All (Urban), RAY etc. as mentioned in items(iv) and (v) of Entry 3 of Notification 11/2017-CT (R), prior to 31-3-2019, whether an option is available to the Promoter to pay the tax at the new rates of 1% or 5% (without ITC) or at the existing rates of 8% (with ITC)?	Yes. The Promoter has the option to pay tax either at the old rate of 8% (with ITC) or at 1% (without ITC) on construction of residential apartments in ongoing projects being constructed under PMAY and other specified housing schemes of the Central or State Governments in items (iv) and (v) of Entry 3 of Notification 11/2017-Central Tax (Rate) dated 28-6-2017. The option to pay tax on construction of apartments in the ongoing projects at the old rates of 8% with ITC has to be exercised by the promoter for ongoing project.
27.	In case where the Development rights are supplied by the Landowner to the Promoter, under an area sharing arrangement between 1st July, 2017 and 31-3-2019, but the allotment of constructed area in an ongoing project is made by the Promoter to the Landowner on or after 1-4-2019, whether the tax liability, if any, is required to be discharged in terms of the Notification No. 4/2018-CT (R)?	Yes. Tax liability on service by way of transfer of development rights prior to 1-4-2019 is required to be discharged in terms of Notification No. 4/2018-Central Tax (Rate) dated 25-1-2018.

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Sr. No.	*Question*	*Answer*
28.	Whether the GST is leviable on the output supply of Transferrable Development Rights by a developer (usually evidenced by TDR Certificate issued by the authorities). If yes, under which entry and at what rate?	Yes, GST is payable on Transfer of Development Rights by a developer to another developer or promoter or to any other person under reverse charge mechanism @ 18% with ITC under Sl. No. 16, item (iii) of Notification No. 11/2017-Central Tax (Rate) dated 28-6-2017 (heading 9972).
29.	What is the meaning of the term "first occupation" referred to in clauses (i) to (id) of Entry 3 of Notification No. 3/2019? Whether, in case of an ongoing project, where part occupation certificate has been received in respect of some of the premises comprised in the ongoing project, the Promoter is entitled to exercise the option of 1%/5% (without ITC) or @ 8%/12% (with ITC) available in terms of Notification No. 3/2019 CT (R), in respect of the balance ongoing project?	The term "first occupation" appearing in Schedule II para 5(b) and in notification No. 11/2017-Central Tax (Rate) dated 29-3-2019 means the first occupation of the project in accordance with the laws, rules and regulations laid down by the Central Government, State Government or any other authority in this regard. Where occupation certificate has been issued for part(s) of the project but not for the entire project by 31-3-2019, the first occupation of the project shall not be considered to have taken place on or before 31-3-2019 and the project shall be considered ongoing project provided it satisfies the other requirements of the definition of the term ongoing project. Promoter shall be entitled to exercise option to pay tax @ 1%/5% (without ITC) or @ 8%/12% (with ITC) on construction of apartments in such project.
30.	(a) In case of a single building registered as 2 (two) separate projects under the provisions of RERA *viz*. 1st to 10th floor as one Project and 11th to 20th floor as another project, whether the Developer can consider the entire building as single ongoing project, since all the three conditions to be complied with for classifying a project as an ongoing project can be satisfied only if the entire building is considered as a single project? (b) Furthermore, if different towers in a single layout are registered as separate projects under the provisions of RERA but where the approvals are common	(a) Both the projects registered as separate projects under RERA, 2016 shall be treated as distinct projects for the purpose of Notification No. 11/2017-Central Tax (Rate) dated 28-6-2017 as amended by Notification No. 3/2019-Central Tax (Rate) dated 29-3-2019. Both the projects will have to independently satisfy the requirements of the definition of ongoing projects. (b) No. All the towers registered as different projects under RERA shall be treated as distinct projects. Only such towers registered as distinct projects for which commencement certificate has been issued on or before 31-3-2019,

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Sr. No.	*Question*	*Answer*
	for all the towers, whether the Developer can consider entire layout as a single ongoing project?	construction has started on or before 31-3-2019 and for which apartments have been booked on or before 31-3-2019 but completion certificate has not been issued or first occupation has not taken place by the said date shall be treated as ongoing projects.
31.	Whether TDR purchased on or after 1-4-2019 to be consumed by a developer-promoter in an ongoing project, in respect of which the promoter has opted for the new rate of tax, shall be liable to be taxed at the applicable rate, but limited to 1% or 5%, as the case may be, of the unsold area at the time of issuance of completion certificate?	Yes. Portion of such TDR transferred on or after 1-4-2019 which is used in an ongoing project in respect of which the promoter has opted for new rate of tax on construction of apartment @ 1% or 5% without ITC which remained unbooked on the date of issuance of completion certificate or first occupation of the project shall be liable to tax at the applicable rate not exceeding 1% of the value in case of affordable residential apartments and 5% of the value in case of other than affordable residential apartments.
32.	What shall be the classification of and rate of tax applicable to works contract service provided by a contractor to a developer or promoter under the new dispensation effective from 1-4-2019 for (a) New project after 1-4-2019 and ongoing projects where option has been exercised for new rate and (b) Ongoing projects where option has not been exercised for new rate?	The rate of tax applicable on the work contract service provided by a contractor to a promoter for construction of a real estate project shall be 12% or 18% depending upon whether such work contract service is provided for construction of affordable residential apartments or residential apartments other than affordable residential apartments. Rate of tax applicable on such work contract service provided by a contractor to a promoter on construction of commercial apartments shall be 18% (irrespective of option exercised by developer-promoter). The relevant entries of the notification are at items (iv), (v), (va) and (vi) against sl. no. 3 of the table in Notification No. 11/2017-Central Tax (rate) dated 28-6-2017 prescribing rate of 12% for works contract services of construction of affordable apartments/apartments being constructed under schemes specified therein. In case of works contract services for construction of other apartments, rate of 18% as prescribed in item (xii) against

Sr. No.	*Question*	*Answer*
		sl. no. 3 of the table in Notification No. 11/2017-Central Tax (rate) dated 28-6-2017 shall be applicable.
33.	A registered project has three blocks and Completion Certificate has been received for one block prior to 1st April, 2019 and for two blocks will be received after that date. Will such a project for which multiple completion certificates are received partly before 1st April, 2019 and partly after that date, constitute an ongoing project?	Where more than one completion certificate is issued for one project, for the purpose of definition of ongoing project as defined in the clause (xx) in the paragraph 4 of the notification No. 11/2017-CTR, dated 28-6-2017, completion certificate issued for part of the project shall not be considered to have been issued for the project on or before 31-3-2019 unless completion certificate(s) have been issued for the entire project. Therefore, if completion certificate has not been issued for part of the project on or before 31-3-2019, the project shall still be considered as ongoing project provided other conditions of the definition of "ongoing project" are met.
34.	It is a prevalent practice that more than one commencement certificate is issued by competent authority for single project. For example, in case of a single tower comprising of 50 floors and registered as single project, separate commencement certificates may be issued by the competent authority for i) basement and parking which is common to entire building (ii) first twenty floors (iii) next thirty floors. If one or two commencement certificates are received by the Developer prior to 1st April, 2019 and remaining on or after that date, will such a project be considered as an ongoing project?	Where commencement certificate has been issued even for part of the project on or before 31-3-2019, it shall be treated as an ongoing project provided other requirements of the definition of ongoing project are met.
35.	There are many projects of redevelopment/ slum rehabilitation in pipeline as on 1st April, 2019. It is possible that in such projects the development rights have been conferred upon the developer and pursuant to which the development process has been initiated such as receipt of commencement certificate, excavation for foundation etc., but booking against units for sale has not been received prior to 1st April, 2019.	In case of redevelopment or slum rehabilitation projects, the original inhabitants or the slum dwellers are not required to pay any monetary consideration to the promoter for the residential apartments allotted to them. Therefore, the residential apartments allotted to the original inhabitants in case of redevelopment project or slum dwellers in case of slum rehabilitation or redevelopment project, the requirement that

Sr. No.	*Question*	*Answer*
	However, allotment of units to the existing dwellers (in respect of free supply units) which will yield no monetary consideration has been done. Clause (xiii) of Para 4 of Notification No. 11/2017-CTR as amended by Notification No. 3/2019-CTR requires credit of at least one instalment in the bank account prior to 1st April, 2019 for a project to be considered as ongoing project. It may please be clarified whether in such cases, apartments being constructed in the project shall be deemed to have been booked prior to 1st April, 2019 in case development agreement is executed prior to that date and whether accordingly such projects shall be considered as an ongoing project?	at least one instalment has been credited to the bank account of the promoter shall not be required to be met for such apartments to be considered as having been booked on or before 31-3-2019 provided other requirements for considering an apartment booked on or before 31-3-2019 have been met. The consideration for such apartments is receipt in the form of transfer of development rights from the original inhabitants in case of redevelopment projects or the government in case of slum rehabilitation projects. Hence, the condition relating to credit of at least one instalment in the bank account of the promoter for the apartments being constructed in a slum redevelopment project to have been partly or wholly booked shall be deemed to have been satisfied in order to consider the project as an ongoing project, provided all other conditions for considering an apartment as booked are met in case of apartments allotted to slum dwellers; as there is no cash payment to be made by the slum dwellers.
36.	Can a developer take deduction of actual value of Land involved in sale of unit instead of taking deduction of deemed value of Land as per Paragraph 2 to Notification No. 11/2017-CTR ?	No. Valuation mechanism prescribed in paragraph 2 of the notification No. 11/2017-CTR dated 28-6-2017 clearly prescribes one-third abatement towards value of land.
37.	Para 3 of Annexure I and II to Notification No. 3/2019-CTR dated 29-3-02019, stipulate three different conditions. Clause (i) and (ii) of the said Para 3 are relating to percentage of invoicing. It is requested to clarify as to how and where the percentage of invoicing is to be taken into consideration while determining quantum of ITC reversal.	The illustrations given in the said annexure clearly explain how the provisions given in the clause (i) and (ii) of para 3 of the said annexure relating to percentage of invoicing shall operate. The same may be referred to.
38.	It may be clarified whether exemption granted on transfer of development right or FSI for residential construction and reverse charge mechanism prescribed for payment of tax on TDR, FSI or long term lease (premium)	The new dispensation has been prescribed for real estate sector *vide* notifications issued on 29-3-2019. The same are effective prospectively from 1-4-2019. They shall apply only to development rights or FSI

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Sr. No.	*Question*	*Answer*
	in the new dispensation is applicable where development rights were transferred by way of an agreement executed prior to 1st April, 2019 but consideration, whether in cash or other form, flowed to the land owner, in full or part, on or after 1st April, 2019.	transferred on or after 1-4-2019. They shall not apply to development rights transferred by way of an agreement prior to 1-4-2019 even if the consideration for the same, in cash or kind, is paid in part or full on or after 1-4-2019.
39.	Land Owner being an individual is not engaged in the business of land relating activities and thus whether the transfer of development rights by an individual to a promoter is liable for GST and whether the same will fall within the scope of "Supply" as defined in Section 7 of CGST/SGST Act, 2017? Position of such a transaction may be clarified in light of amendments recently made.	The term business has been assigned a very wide meaning in the CGST Act and it includes any trade, commerce, manufacture, profession, vocation, adventure, or any other similar activity whether or not it is for a pecuniary benefit irrespective of the volume, frequency, continuity or regularity of such activity or transaction. Therefore, the activity of transfer of development rights by a land owner, whether an individual or not, to a promoter is a supply of service subject to GST.
40.	In certain projects, developers have started construction on or before 31-3-2019. However, bookings in the project have not started. One of the conditions prescribed for a project to qualify as an ongoing project is that apartments being constructed should have been partly or wholly booked. Whether such project where bookings have not started but construction has started, would be eligible for the new rates of 1% or 5% without ITC?	As per explanation in clause (xxviii) of para 4 of the notification No. 11/2017-CTR dated 28-6-2017, "project which commences on or after 1-4.2019" shall mean a project other than an ongoing project. A project, in which bookings for the apartments have not started, would not be covered under definition of "ongoing project". The same would accordingly be treated as a project which commences on or after 1-4-2019 subject to the new rates of 1% or 5% without ITC, as the case may be.
41.	Whether the Form as per Annexure IV of the Notification No. 3/2019-CTR is to be filed with both the Jurisdictional commissioner i.e. Central Tax, State Tax. Whether modifications/amendments in such Form are allowed subsequent to filing of the form, after 10th May, 2019?	No. The Form shall be filed manually with the office of the Commissioner in whose jurisdiction the registration of the promoter is assigned. No modification/amendment of the option is allowed in the Form once submitted.

GSTN FAQs

About Form GSTR-9A – GST CORNER

1. **What is Form GSTR-9A?**
   Form GSTR-9A is an annual return to be filed once, for each financial year, by taxpayers who have opted for composition scheme, for any period during the said financial year. The taxpayers are required to furnish details regarding outward supplies, inward supplies, taxes paid, any refund claimed or demand created or input tax credit availed or reversed due to opting out or opting in to composition scheme.

2. **Who needs to file Form GSTR-9A?**
   All taxpayers registered under the composition scheme under GST, for any period during the financial year, need to file Form GSTR-9A. This will include a taxpayer –
   - who has opted in for composition scheme since registration and have never opted out subsequently; and
   - who have opted in for composition scheme any time during the financial year; and
   - who have opted in for composition but subsequently opted out any time during the year.

3. **Who doesn't need to file Form GSTR-9A?**
   Following persons are not required to file Form GSTR-9A:
   - Regular taxpayer who has not opted in composition scheme for any period during the financial year
   - Non-resident taxable persons
   - Input service distributor
   - Casual Taxable Person
   - Persons required to Deduct Tax at Source u/s. 51
   - Persons required to Collect Tax at Source u/s. 52

4. **Is it mandatory to file Form GSTR-9A?**
   Yes, it's mandatory to file Form GSTR-9A for composition taxpayers.

5. **I am a regular/normal taxpayer for part period and composition taxpayer for part period during the financial year. Do I need to file Form GSTR-9 or Form GSTR-9A?**
   You are required to file both Form GSTR-9 and Form GSTR-9A.

   The period during which the taxpayer remained as composition taxpayer, Form GSTR-9A is required to be filed. And, for period for which the taxpayer is registered as normal taxpayer, Form GSTR-9 is required to be filed.

   For example: If the taxpayer was registered as a normal taxpayer during period 1st July, 2017 to 31st December, 2017, then for such period Form GSTR-9 is required to be filed. And, if the taxpayer had opted for Composition scheme from 1st January, 2018 to 31st March, 2018, then Form GSTR-9A is required to be filed for such period i.e. (Jan-March, 2018).

   Both Form GSTR-9 and Form GSTR-9A for the respective period are required to be filed for FY 2017-18, in such cases.

6. **I got my registration cancelled in the financial year. Can I file Form GSTR-9A?**
   The annual return can be filed even if the taxpayer has got his registration cancelled during the said financial year.

Opt in and Opt out of composition & Form GSTR-9A

7. **I opted out of composition scheme in the financial year. Do I need to file Form GSTR-9A?**
   Taxpayers who have opted out from the composition scheme need to file Form GSTR-9A for the period during which they were registered under the composition levy scheme.

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Pre-conditions of Filing Form GSTR-9A

8. **What are the pre-conditions for filing Form GSTR-9A?**
   Pre-conditions for filing of Form GSTR-9A are:
   - Taxpayer should have been registered in the relevant financial year and opted for composition scheme for even a day during the financial year.
   - Taxpayer has filed all applicable returns i.e., Form GSTR-4, quarterly return of the relevant financial year, before filing the Annual Return.

Filing Nil Form GSTR-9A

9. **Can I file Nil Form GSTR-9A?**
   Nil Form GSTR-9A can be filed for the Financial year, if you have:–
   - NOT made any outward supply (commonly known as sale); AND
   - NOT received any goods/services (commonly known as purchase); AND
   - NO other liability to report; AND
   - NOT claimed any credit; AND
   - NOT claimed any refund; AND
   - NOT received any order creating demand; AND

   There is no late fee to be paid etc.

Filing Form GSTR-9A

10. **How can I as a taxpayer file Form GSTR-9A?**
    Navigate to Services > Returns > Annual Return to file Form GSTR-9A.

11. **Can the date of filing of Form GSTR-9A be extended?**
    Yes, date of filing of Form GSTR-9A can be extended by Government through notification.

12. **Are values in different tables of Form GSTR-9A auto calculated based on Form GSTR-4?**
    GST Portal calculates the GSTR-9A values in different tables, based on Form GSTR-4 filed by you. This is also available as download in PDF format and will be auto populated in different tables as well in Form GSTR -9A, in editable form.

13. **Form GSTR-9A return is required to be filed at entity level or GSTIN level?**
    Form GSTR-9A return is required to be filed at GSTIN level i.e., for each registration. If taxpayer has obtained multiple GST registrations, under the same PAN, whether in the same State or different States, he/she is required to file annual return for each registrations separately, where the GSTIN was under composition scheme for some time during the financial year or for the whole of the financial year.

14. **I have not filed all my applicable return(s)/statement(s) during the financial year. Still, can I file Annual return without filing of those applicable return(s)/statement(s)?**
    No. You cannot file return in Form GSTR-9A without filing Form GSTR-4 for all applicable periods during the relevant financial year.

Entering Details in Tables of Form GSTR-9A

15. **In which tables of Form GSTR-9A, the details are required to be provided?**
    Details are required to be provided in Form GSTR-9A in the following tables:

    1. **6. Details of Outward supplies made during the financial year:** To enter/view the summary of outward supplies made during the financial year

2. **7. Details of inward supplies on which tax is payable on reverse charge basis (net of debit/credit notes) for the financial year:** To enter/view the summary of inward supplies liable to reverse charge for the financial year

3. **8. Details of other inward supplies for the financial year:** To enter/view the summary of other inward supplies for the financial year

4. **9. Details of tax paid as declared in returns filed during the financial year:** To enter/view the tax (including Interest, Late Fee, Penalty & Others) paid as declared during the financial year

5. **10, 11, 12 & 13. Particulars of the transactions for the previous FY declared in returns of April to September of current FY or up to date of filing of annual return of previous FY whichever is earlier:** To enter the summary of transactions declared in next financial year

6. **14. Differential tax paid on account of declaration made in 10, 11, 12 & 13 above:** To enter/view the total tax paid on transactions reported in next financial year

7. **15. Other information – Particulars of Demands and Refunds:** To enter/view the particulars of demands and refunds during the financial year

8. **16. Details of credit reversed or availed:** To enter/view the summary of credit reversed or credit availed on opting in and/or opting out of composition scheme

16. Which tables in Form GSTR-9A has auto-populated data from filed Form GSTR-4?

Below tables in Form GSTR-9A has auto-populated data from filed Form GSTR-4:

1. 6. Details of Outward supplies on which tax is payable as declared in returns filed during the financial year

2. 7. Details of inward supplies on which tax is payable on reverse charge basis (net of debit/credit notes) declared in returns filed during the financial year

3. 8. Details of other inward supplies as declared in returns filed during the financial year

4. 9. Details of tax paid as declared in returns filed during the financial year

17. Can I edit auto-populated details in Form GSTR-9A?

Yes, you can edit auto-populated data in form GSTR-9A except tax paid column of Table No. 9. The outward supplies details can be edited in order to indicate actual supplies made and not merely outward supplies indicated in the Returns.

18. Do I need to provide information relating to all supplies made during the financial year?

Yes, you need to provide information relating to all supplies made during the financial year and not merely the supplies reported in the return.

19. Can I download system computed values of Form GSTR-9A?

Yes, taxpayer can download the system computed values for Form GSTR-9A in PDF format. This will help the taxpayer to use it as reference while filling Form GSTR-9A.

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Form GSTR-9A & Consolidating Summary

20. Will consolidated summary of Form GSTR-4 be made available for the returns filed during the financial year?

Yes. Consolidated summary of all filed Form GSTR-4 statement for the relevant financial year is available for download in PDF format. Navigate to Services > Returns > Annual Return > Form GSTR-9A (PREPARE ONLINE) > DOWNLOAD GSTR-4 SUMMARY (PDF) option.

21. By when do I need to file Form GSTR-9A?

The due date for filing Form GSTR-9A for a particular financial year is 31st December of subsequent financial year or as extended by Government through notification from time-to-time.

Filing & Paying Late Fee

22. What happens after COMPUTE LIABILITIES button is clicked?

After COMPUTE LIABILITIES button is clicked, details provided in various tables are processed on the GST Portal at the back end and Late fee liabilities, if any, are computed. Late fee is calculated, if there is delay in filing of annual return beyond due date.

23. Is there any late fee for late filing of Form GSTR-9A?

Yes, there is a late fee for filing of Form GSTR-9A beyond the due date.

24. Can I file form GSTR-9A return without paying late fee (if applicable)?

No. You can't file Form GSTR-9A without payment of late fee for Form GSTR-9A, if same is filed after the specified date.

25. Is there any option to make payment other than late fee (if applicable) in Form GSTR-9A?

After filing of your return in Form GSTR-9A, you will get link to navigate to Form GST DRC-03 to pay tax, if any. Any additional payment can be made using Form GST DRC-3 functionality only and that too by cash.

Additional Liability & it's Payment

26. In form GSTR-9A, can additional liability not reported earlier in Form GSTR-4 be declared?

Yes, additional liability not reported earlier at the time of filing Form GSTR-4 can be declared in Form GSTR-9A. The additional liability so declared in Form GSTR-9A are required to be paid through Form GST DRC-03.

27. What do I need to do if available cash balance in Electronic Cash Ledger is less than the amount required to offset the liabilities?

Available cash balance as on date in Electronic Cash Ledger is shown to the taxpayer in "Cash Ledger Balance" table. If available cash balance in Electronic Cash Ledger is less than the amount required to offset the liabilities, then additional cash required to be paid by taxpayer is shown in the "Additional Cash Required" column. You may create challan for the additional cash directly by clicking on the **CREATE CHALLAN** button.

Previewing & Signing Form GSTR-9A

28. Is there any Offline Tool for filing Form GSTR-9A?

Yes, offline tool is available for Form GSTR-9A. However, filing can take place only online on the GST Portal.

Using Offline Utility, you will be able to open the system-computed Form GSTR-9A based on filed Form GSTR-4 for editing as well as to prepare details of Table 6 to Table 16 of Form GSTR-9A. Once you have uploaded the prepared

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details on the GST Portal, you must file return on the portal with your Login credentials.

29. What are the modes of signing Form GSTR-9A?

You can file Form GSTR-9A using DSC or EVC.

(a) Digital Signature Certificate (DSC)

Digital Signature Certificates (DSC) are the digital equivalent (that is electronic format) of physical or paper certificates. A digital certificate can be presented electronically to prove one's identity, to access information or services on the Internet or to sign certain documents digitally. In India, DSC are issued by authorized Certifying Authorities.

The GST Portal accepts only PAN based Class II and III DSC.

To obtain a DSC, please contact any one of the authorised DSC-issuing Certifying Authorities: http://www.cca.gov.in/cca/?q=licensed_ca.html.

(b) Electronic Verification Code (EVC)

The Electronic Verification Code (EVC) authenticates the identity of the user at the GST Portal by generating an OTP. The OTP is sent to the mobile phone number of the registered mobile phone of Authorized Signatory filled in part A of the Registration Application.

30. I am getting a warning message that records are under processing or processed with error while filing Form GSTR-9A. What do I do?

In case, records (or data as submitted while filing Form GSTR-9A) are processed with error or are under processing at the back end, a warning message is displayed. If records are still under processing, wait for processing to be completed at the back end. For records which are processed with error, go back to Form GSTR-9A and take action on those records.

31. Can I preview Form GSTR-9A before filing?

Yes, you can view/download the preview of Form GSTR-9A in PDF and Excel format by clicking on 'PREVIEW DRAFT GSTR-9A (PDF)' and 'PREVIEW DRAFT GSTR-9A (EXCEL)' button before filing Form GSTR-9A on the GST Portal.

Post Filing of Form GSTR-9A

32. Can I revise Form GSTR-9A return after filing?

No, you cannot revise Form GSTR-9A return after filing.

33. What happens after Form GSTR-9A is filed?

After Form GSTR-9A is filed:

- ARN is generated on successful filing of the return in Form GSTR-9A.
- An SMS and an email is sent to the taxpayer on his registered mobile and e-mail id.
- Electronic Cash ledger and Electronic Liability Register Part-I will get updated on successful set-off of liabilities (late fee only).
- Filed form GSTR-9A will be available for view/download in PDF and Excel format.

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CA Naresh Sheth & CA Jinesh Shah

INDIRECT TAXES

GST – Recent Judgments and Advance Rulings

A. Writ Petitions

1. M/S. MEGHA ENGINEERING & INFRASTRUCTURE LTD – HIGH COURT OF TELANGANA (2019-TIOL-893-HC-TELANGANA-GST)

Facts, Issue involved and Contention of Petitioner

Petitioner is a manufacturer of MS Pipes and is involved in execution of various infrastructure projects. Under the GST legislation, assessees are required to file return in Form GSTR-3B on or before the 20th of every month, for discharge of their liability of the previous month. The GST liability is permitted to be discharged by utilising the available ITC balance.

The case of the petitioner is that the GST portal is designed in such a manner that unless assessee discharges the entire tax liability, the system will not accept the return in Form GSTR-3B. As a result, even if an assessee is entitled to set off, to the extent of 95%, by utilising the ITC, the return cannot be filed unless the remaining 5% is paid in cash.

There was a delay on part of petitioner in filling the form GSTR-3B for the period from October, 2017 to May, 2018. Total tax liability of the petitioner for the period from July, 2017 to May, 2018 was ₹ 10,140,289,385/- and the ITC available to the credit of the petitioner during this period was ₹ 9,685,886,133/-. Thus, there was a short fall to the extent of ₹ 454,403,252/- which the petitioner was obliged to pay by way of cash. According to the petitioner, they could not make the payment and file the return within time due to certain constraints. However, the entire liability was wiped out in May 2018 along with interest (calculated on net tax liability after ITC set off).

Assistant Commissioner issued a letter to the petitioner demanding payment of interest on full tax liability. Petitioner replied by stating that interest is to be calculated only on the net tax liability after deducting available ITC from the total tax liability and that they have correctly paid an amount of ₹ 30,925,222/- towards interest on net tax liability. However, department demanded interest on total tax liability and hence petitioner preferred a writ petition.

Department filed counter affidavit stating that Section 50 of the Act imposes a burden in the form of interest, upon every person who is liable to pay tax, but failed to pay the same. Liability to pay interest under Section 50(1) is a statutory obligation, which the registered persons are obliged to comply on their own

accord. Section 50(1) is not confined only to the cash component of the tax payable.

Discussions by and Observations of HC

Filing of Return

Section 39 states that every registered person should furnish for every calendar month or part thereof, a return, electronically, of inward and outward supplies of goods or services, ITC availed, tax payable, tax paid etc., on or before the 20th day of the succeeding calendar month

Input Tax Credit

Section 41 deals with the claim of ITC and the provisional acceptance thereof. Under this provision, every registered person is entitled to take the credit of eligible input tax, as self-assessed in his return. The amount claimed shall be credited on a provisional basis to his electronic credit ledger.

The amount available in the electronic credit ledger may be used by virtue of sub-section (4) of Section 49, for making any payment towards output tax under the Act.

As per Section 41(1), a person gets credit of input tax in his electronic credit ledger only upon filing of return on self-assessment basis. Until return is filed, no credit becomes available in the electronic credit ledger. Utilisation of credit for payment of self-assessed tax is permissible only after the credit becomes available in the electronic credit ledger.

Thus, the return filing scheme makes a distinction between (i) the entitlement to take credit, which comes first; (ii) the actual entry of credit in the electronic credit ledger, which comes next; and (iii) the actual payment from out of the credit, which comes last.

There can be no doubt about the fact that even in respect of the input tax credit available in the electronic credit ledger, there is a necessity to make payment. Section 49(2) confirms the stage at which a credit entry is made and Section 49(4) enables a registered person to make payment from out of the credit so available in the electronic credit ledger.

Section 50(1) states that the liability to pay interest arises automatically, when a person who is liable to pay tax, fails to pay the tax to the Government within the period prescribed. The liability to pay interest is in respect of the period for which the tax remains unpaid. In fact, the liability to pay interest under Section 50(1) arises even without any assessment, as the person is required to pay such interest "on his own".

It is clear that the liability to pay interest under Section 50(1) is self-imposed and automatic, without any determination by anyone. Hence, the stand taken by the department that the liability is compensatory in nature, appears to be correct.

Once it is clear that the liability to pay interest arises for non-payment within the period prescribed, we should see (i) what is the period prescribed for payment of tax, and (ii) the mode of such payment.

The period prescribed for payment of tax in respect of every month is on or before the 20th day of the succeeding calendar month.

Section 49(2) states that credit entry is made in the electronic credit ledger of a registered person, only when the ITC, as self-assessed, is found in the return of a registered person. After credit entry is made in the electronic credit ledger, the same becomes available for making payment. This is clear from sub-section (3) of Section 49.

In other words, until a return is filed as self-assessed, there is no entitlement to credit and no actual entry of credit in the electronic credit ledger. As a consequence, no payment can be made from out of such a credit entry.

It is true that the tax paid on the inputs charged on any supply of goods and/services, is always available. But, it is available in the air or in the cloud. Just as information is available in the server and it gets displayed on the screens of our computers only after connectivity is established, the tax already paid on the inputs, is available in the cloud. Such tax becomes an input tax credit only when a claim is made in the returns filed as self-assessed. It is only after a claim is made in the return that the same gets credited in the electronic credit ledger. It is only after a credit is entered in the electronic credit ledger that payment could be made, even though the payment is only by way of paper entries.

If we take a common example of banking transactions, this can be illustrated much better. An amount available in the account of a person, though available with the bank itself, is not taken to be the money available for the benefit of the bank. Money available with the bank is different from money available for the bank till the bank is allowed to appropriate it to itself.

Admittedly, the petitioner has filed returns belatedly. Payment of the tax liability, partly in cash and partly in the form of claim for ITC was made beyond the prescribed period. Therefore, the liability to pay interest under Section 50(1) arises automatically. The petitioner cannot, therefore, escape from this liability.

Only when the payment is so made, the Government gets a right over the money available in the ledger. Since ownership of such money is with the dealer till the time of actual payment, the Government becomes entitled to interest up to the date of their entitlement to appropriate it.

Decision of HC

Petitioner is liable to pay interest on gross amount. There is no fault in claim made by the respondents for interest on the ITC portion of the tax.

2. M/s. SAFARI RETREATS PVT. LTD. AND ANOTHER VS CHIEF COMMISSIONER OF CGST AND OTHERS – HIGH COURT OF ORISSA (2019-TIOL-1088-HC-ORISSA-GST)

Facts, Issue involved and Contention of the Petitioner

Petitioner is engaged in business of construction of shopping malls for letting out the same to numerous tenants and lessees. Petitioner uses huge quantities of material and other inputs for the construction of mall. Input goods for the petitioner includes cement, sand, steel, aluminium, wires, plywood, paints, lifts, etc. They also receive input services like consultancy services, legal services, architectural services, etc., for the purpose of completion of construction. The above goods and services purchased for the construction of mall are taxable under GST and they have to pay huge amount of CGST (Central Goods and Services Tax) and OGST (Orissa Goods and Services Tax) on such procurements.

After construction of the mall, the petitioner has made the necessary arrangements for letting out of units of the shopping mall to different persons on rental basis. Letting out of units of the shopping mall is squarely covered u/s. 7, i.e., "Supply" and therefore attracts GST.

Petitioner having huge accumulated Input Tax Credit (ITC) from the purchases of input goods and services is desirous of availing the ITC to discharge the outward GST liability on the rentals received from the tenants.

Petitioner was, however, advised to deposit the CGST and OGST collected from the customers without utilizing the ITC in view of restrictions u/s. 17(5)(d) of the CGST Act. Section 17(5)(d) prescribes that Input

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Tax Credit shall not be available in respect of the goods and services or both received by a taxable person for construction of an immovable property (other than plant or machinery) on his own account including when such goods or services or both are used in the course or furtherance of business. Therefore, the petitioner has challenged the provisions of Section 17(5)(d) in the case of immovable property intended to be let out for rent.

Petitioner's submissions

Petitioner placed reliance on the decision of the Honourable Supreme Court Judgment in the case of *Eicher Motors Ltd. vs. Union of India* wherein it was held that –

"A right accrues to the assessee on the date when they paid the taxes on the inputs i.e. raw materials and the right would continue until the facility available thereto gets worked out or until those goods exists."

It is pertinent to note that rights accrued during the existing law (pre-GST regime) are specifically saved under Section 174 of the CGST Act, 2017, which would include the right to pass on the CENVAT credit and such an accrued right cannot, therefore, be taken away and in the manner done. On the point of promissory estoppel, attention was invited to judgments in the compilation and particularly the principle emerging from the Judgment in *Motilal Padampat Suresh 20-21-WPGOJ-3142.2017.doc Sugar Mills Co. Ltd. vs. State of Uttar Pradesh & Others, reported in (1979) 2 SCC 409.*

Petitioner also relied on the judgment of *'Dai Ichi Karkaria Ltd'* wherein it is held that –

"CENVAT is an indefeasible right of the assessee and it is vested on him at the point of time when he utilizes the input service for service provided or to be provided."

The Petitioner also submitted Government Circular dated 8-12-2018 – Effective tax rate on complex, building, flat, etc., Relevant extract is as under:

"It is brought to the notice of buyers of constructed property that there is no GST on sale of complex/ building and ready to move-in flats where sale takes place after issue of completion certificate by the competent authority. GST is applicable on sale of under construction property or ready to move-in flats where completion certificate has not been issued at the time of sale."

Discussions by and observations of HC

The High Court observed that the sale of immovable property post issuance of completion certificate does not attract GST. Since there is a break in the tax chain, ITC is denied as GST is not payable on the same. However, the position is completely different where the immovable property is constructed for letting out because the tax chain is not broken. In fact, the construction of the building will result in fresh stream of GST revenues to the exchequer of the Government.

Denial of ITC in respect of building which is meant and intended to be let out would amount to treat it as identical to a building which is meant and intended to be sold. Same treatment for these two different buildings is contrary to the basic principles regarding classification of subject matter for the levy of tax and therefore violates Article 14 of the Constitution.

Further, the GST authorities are themselves reading down Section 17(5)(d) and presuming it as inapplicable to a builder who sells units in the building before the issuance of a completion certificate and who is required to pay CGST/OGST on the amount of sale price received by him. To grant input tax credit to a builder who sells building where completion certificate has not been issued at the time of sale while **denying it to a person**

like the petitioner is patently and egregiously arbitrary and discriminatory. Further, such an interpretation of Section 17(5)(d) of both CGST and OGST Act leads to double taxation, i.e., firstly, on the inputs consumed in the construction of the building and secondly, on the rentals generated by the same building.

It is also a settled-principle of interpretation of tax-statutes that interpretation should be adopted which avoids double taxation. It would also be violative of the Petitioners' fundamental right to carry on business under Article 19(1)(g) of the Constitution as it would impose a wholly unwarranted, unreasonable and arbitrary restriction which would render buildings now constructed for letting out uncompetitive, by imposing the burden of double taxation.

Decision of HC

The High Court observed that the very objective of the GST Act is to make uniform the provision for levy, collection of tax, intra-State supply of goods and services and avoid multi-taxation. In this case, the petitioner is renting the units of shopping mall on which he is liable to discharge GST. However, the petitioner is deprived of utilizing huge accumulated ITC for payment of output GST liability.

The Court observed that the narrow construction of interpretation of the Section 17(5)(d) by the department is frustrating the very objective of the Act. Court was of the view that the provisions of Section 17(5)(d) is to be read down and the narrow restriction as imposed in reading of the provision by the department is not accepted. The Court relied on the judgment of *Eicher Motors Ltd. (2002-TIOL-149-SC-CX-LB)* wherein it was held that the very purpose of the credit is to give benefit to the assessee. Hence, the petitioner should be allowed to utilise ITC irrespective of the prohibition of Section 17(5)(d) to discharge his output liability. Therefore, the prayer by the petitioner is granted.

B. Rulings by Appellate Authority of Advance Ruling

3. BENGAl PEERLESS HOUSING DEVELOPMENT COMPANY LTD – AAR MAHARASHTRA (2019-TIOL-137-AAR-GST)

Facts, Issue involved and Query of the Applicant

Applicant is a joint venture of the West Bengal Housing Board and the Peerless General Finance and Investment Company Limited for developing real estate projects in West Bengal. It is developing a residential housing project named 'Avidipta II' and supplying construction service to the recipients for possession of dwelling units in the year 2023. In addition to the construction service, the Applicant provides services like preferential location service which includes services of floor rise and directional advantage.

Applicant has sought advance ruling for the following

1. *Whether the supply of preferential location service which includes services of floor rise and directional advantage constitutes a composite supply with construction service as the principal supply?*
2. *If so, whether abatement is applicable on the entire value of the composite supply.*

Applicant's submissions

Applicant provides construction service to a recipient only after the agreement is signed and other terms and conditions laid down in the agreement are fulfilled. It is, therefore, absolutely clear from the context that the construction service is being provided only with respect to the dwelling unit allotted and after the allotment money paid.

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Supply of construction service cannot, therefore, be separated from the supply of the services of directional advantage and benefit of floor rise associated with the unit allotted to the recipient. Supply of construction service is, therefore, naturally bundled with the supply of the services of directional advantage and benefit of floor rise, and all of them are being supplied in conjunction with one another in the ordinary course of business. It is, therefore, a composite supply with construction supply, being the dominant element, as the principal supply.

Discussions by and observations of AAR

Agreement refers to the sale of an immovable property. It is relevant so far as construction service (SAC 9954) is offered, assuring coming into being of the immovable property. The buyer also pays in advance for certain other services that he will enjoy after obtaining possession of the property (for e.g., Preferential location services, car parking space, etc.). The buyer agrees to pay a single consolidated amount for all these supplies. The question that needs to be examined is whether they are naturally bundled and are supplied in conjunction with one another in the ordinary course of business and whether the construction supply is the dominant element and all other services in the bundle are ancillary or incidental to the supply of the construction service.

Although actual provisioning of the construction and other services are made at different points of time, they can be supplied in a bundle. This is because supply, as defined under Section 7(1) of the GST Act, includes agreement to supply even if actual supply is to be made at a future date, provided and to the extent, the recipient pays in advance. There is no straightjacket formula to examine whether they are naturally bundled and supplied in conjunction with one another in the ordinary course of business.

Services that are naturally bundled can be treated as provisioning of a single service that lends the bundle its essential character. It is the predominant element of the combination of services being supplied. Whether the services so bundled are provided in conjunction with one another in the ordinary course of business would depend upon the normal or frequent practices adopted in a business and can be ascertained from several indicators.

Section 2(30) of the GST Act draws upon these concepts to define composite supply as supply by a taxable person of a combination of taxable goods or services or both, which are naturally bundled and supplied in conjunction with one another in the ordinary course of business, where one of the supplies can be identified as the principal supply. Section 2(90) of the GST Act defines principal supply as the predominant element of such a composite supply where all other supplies in the bundle are ancillary to the principal supply.

In the instant case, the nature of construction services is such that it may be treated as the main supply and the other supplies combined with such main supply are in the nature of incidental or ancillary services. Thus, construction services get the character of predominant supply over other supplies.

Supply of construction service is treated as principal supply and therefore the rate applicable on such composite supply (bundle) shall be the rate attributable to the construction service.

Ruling of AAR

In respect of question (1), the applicant is providing a composite supply of the bundle of services described above.

In respect of question (2), construction service being the principal supply, entire value of the composite supply is to be treated for the

purpose of taxation at the rate mentioned above.

4. RAMBAGH PALACE HOTELS PRIVATE LIMITED – AAR RAJASTHAN (2019-TIOL-155-AAR-GST)

Facts, Issue involved and Query of the Applicant

Applicant is a five star deluxe heritage hotel. It is engaged in hospitality business under the brand name 'Taj group'. It is providing Short term accommodation service, restaurant service, mandap keeper service, SPA and other club facilities, etc. which is taxable under GST. In order to maintain its brand image, applicant constantly incurs expenditure on construction, renovation, repairs and maintenance of hotel's immovable and movable property. Major portion of expense is towards repair and maintenance of the hotel.

Applicant has sought advance ruling for following questions

1. *Building Repair Works*
   a. *Whether GST paid on building materials, such as cement, concrete, bricks, cement or marble or stone slabs or tiles, paint, polish and any other building materials meant for repair of building shall be available as ITC?*
   b. *Whether GST paid on labour supply for carrying out repair of building shall be available as ITC, where material and supervision is provided by the applicant?*
   c. *Will it make any difference if aforementioned works are carried out in a composite manner as a works contract?*

   Being routine repairs, the amount spent on the above mentioned all scenarios are charged to revenue as per accounting standards.

2. ***Repair Work relating to electric installation/Sanitary Fittings***
   a. ***Whether GST paid on electrical fittings, such as Cables, Switches, NCB, and other electrical consumables meant for repair of existing electrical fittings shall be available as ITC?***
   b. ***Whether GST paid on sanitary fittings, such as tiles, commode, bath tub, wash basin, PVC pipes and other bathroom sanitary fittings and consumables meant for repair of existing sanitary fittings shall be available as ITC?***
   c. ***Whether GST paid on labour supply for carrying out repair of electrical installation and/ or sanitary fittings shall be available as ITC, where material and supervision is provided by the applicant?***
   d. ***Will it make any difference if aforementioned works are carried out in a composite manner as a works contract?***

Being routine repairs, the amount spent on the above mentioned all scenarios are charged to revenue as per accounting standards.

3. *Furniture & Fixture repairing work*
   a. *Whether GST paid on wood, board, mica, tapestry, paint, polish and other consumables meant for repair of existing furniture & fixtures shall be available as ITC?*
   b. *Whether GST paid on labour supply for carrying out repair of furniture & fixtures shall be available as ITC, where material and supervision is provided by the applicant?*

c. Will it make any difference if aforementioned works are carried out in a composite manner as a works contract for carrying out repair and maintenance job on movable furniture?

Being routine repairs, the amount spent on the above mentioned all scenarios are charged to revenue as per accounting standards.

Discussions by and observations of AAR

Applicant, in routine manner or as and when required, is involved in repair and maintenance of the building and its components in order to ensure that the high standards of hospitality service are maintained. In a way, the repairs of hotel are for furtherance of business in respect to hospitality and supply of services as mentioned above.

Section 2(119) of CGST Act, 2017 defines "works contract" which means a contract for building, construction, fabrication, completion, erection, installation, fitting out, improvement, modification, repair, maintenance, renovation, alteration or commissioning of any immovable property wherein transfer of property in goods (whether as goods or in some other form) is involved in the execution of such contract.

Nature of work undertaken by the applicant is predominantly for immovable property involving transfer of goods and services, therefore, the activity is works contract for carrying out repair and maintenance work.

Section 16(1) and 16(2) provides for eligibility and allowability of ITC. Further, Section 17 of CGST Act, 2017 debars certain activities/ supplies/work from the eligibility to claim ITC.

As per section 17(5)(c) and 17(5)(d), Input Tax Credit in general is not available for construction, reconstruction, renovation, addition, alteration or repair of an immovable property even when such goods or services or both are used in course or furtherance of business.

Applicant is paying GST on building materials and electrical fittings, such as cement, concrete, bricks, cables, switches, etc. as well on manpower supply engaged by them. This activity of repair & maintenance and installation of electrical and sanitary fittings encompasses supply of goods as well as services for a construction activity is in relation to immovable property. The provisions of ITC for the said supply of goods and services is covered under Section 17(5)(d). Therefore, ITC on GST paid on such goods as well as services will not be available to the extent of capitalisation.

Aforementioned supply of goods and services supplied for construction work of an immovable nature can be done in composite manner also i.e., works contract. The works contract service for supply of above mentioned goods and service is covered under Section 17(5)(c). Therefore, ITC on GST paid on above said works contract service will not be will available to the extent of capitalisation of the said goods or services.

Applicant is paying GST on wood, board, mica, tapestry, for repair of existing furniture & fixtures and buying of new furniture & fixtures such as sofa, table, chairs, etc. The activity of supply of said goods and services of manpower for repair in relation to furniture & fixtures is a composite supply of goods and services. The furniture and fixtures are not immovable property in most cases. In the scenario where, the furniture and fixtures are fixed or immobilised or considered as a part of construction activity of immovable nature then the input tax credit will not be available to the extent of capitalization of such goods and services as per provisions mentioned in Section 17 of CGST/IGST Act, 2017. Applicant can avail ITC of GST paid on purchase of new ready to use furniture such as chairs, etc., as per provisions mentioned in Section 16 of the CGST/IGST Act, 2017.

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Ruling of AAR
In respect of building repair work and electric installation/sanitary fittings work, ITC shall not be available to the extent of capitalization of such expenses.

In respect of Furniture and Fixture repairing work, ITC shall be available in accordance with Section 16 of CGST Act.

5. SENCO GOLD LTD – AAR MAHARASHTRA (2019-TIOL-140-AAR-GST)

Facts, Issue involved and Query of the applicant
Applicant is engaged in the manufacturing and retailing of jewellery and articles made of gold, silver and other precious stones under the brand name "Senco Gold & Diamonds". Applicant maintains a network of franchisee-operated stores.

Applicant raises tax invoice on the franchisee for supply of jewellery and other articles and franchisee also raises tax invoices on the applicant for supply of old gold, silver etc. received by them from the customers.

Applicant intends to settle the mutual debts through book adjustments.

Applicant has sought advance ruling as to "whether the input tax credit is admissible when the debt created on account of inward supplies from the franchisee is settled through book adjustment?"

Applicant's submissions
Applicant draws attention to proviso to section 16(2) of CGST Act which provides for reversal of ITC by recipient on account of failure to make payment to the supplier. Apart from the above proviso, the GST Act nowhere makes availing of input tax credit dependent upon the payment to be made for the inward supply. The captioned proviso also does not prescribe or restrict the mode in which the payment has to be made.

Applicant submits that payment through adjustment of the books of account is a prevalent commercial practice. Para 42 of Indian Accounting Standard 32 provides that a financial asset and a financial liability shall be offset and the net amount presented in the balance sheet when, and only when, an entity (a) currently has a legally enforceable right to set off the recognized amounts; and (b) intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Revenue's contention
Section 49(1) provides that every deposit made towards tax, interest, penalty, fee and any other amount shall be made through internet banking or by using credit or debit cards or NEFT or RTGS or by such other mode and subject to such conditions and restrictions as may be prescribed. Explanation (a) to section 49 further provides that the date of credit to the account of the Government in the authorised bank shall be deemed to be the date of deposit in the electronic cash ledger.

According to the concerned officer, the above provisions make it clear that all transactions of the supplier and the recipient should be made through the online banking system. Therefore, the recipient is ineligible to claim credit of input tax if the payment is made by way of book adjustment instead of through any banking channel.

Discussions by and observations of AAR
Authority found that the section 49(1) deals with the manner in which the supplier shall make payment of tax, interest etc., to the government to be credited to his electronic cash ledger. Applicant has made no submission that he intends to deposit tax to the Government in any manner.

Section 49(2) provides that the input tax credit as self-assessed in the return of the registered person shall be credited to electronic credit

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ledger. It does not prohibit the applicant from reporting in the return input tax credit when consideration is paid to the supplier by way of book adjustment. Section 49 does not deals with the mode of transaction between the recipient and the supplier.

Third proviso to the Section 16(2) of the GST Act says, "The recipient shall be entitled to avail of the credit of input tax on payment made by him of the amount towards the value of supply of goods or services or both along with the tax payable thereon". It clearly limits the recipient's entitlement to input tax credit only to transactions where he has paid the consideration for the supply received, along with the tax payable thereon. Such input tax may be provisionally credited to the recipient's electronic credit ledger, but the same will be reversed according to the second proviso to the section 16(2).

It is, therefore clear the no input tax credit is admissible unless the recipient pays the supplier the consideration for the supply received.

'Consideration', as defined under Section 2(31), provides the scope and ambit for modes of payment. It includes, in relation to the supply of goods or services, any payment, made or to be made, whether in money or otherwise, and also the monetary value of any act or forbearance. This definition of 'consideration' cast the net so wide that almost no form of payment is excluded.

For example, a mix of money and monetary value of the goods offered together with it is a valid 'consideration'. Similarly, if the payee owes the payer a debt, and accepts a reduction in such a debt liability as a valid form of payment, that should also be regarded as a valid 'consideration' for a supply. In other words, reduction in book debt (an asset in the payer's books of account) is a valid 'consideration'.

The above discussion establishes that the recipient can pay the supplier consideration by way off-setting off book debt. Unless the law specifically restricts the recipient from claiming the input tax credit when the consideration is paid through book adjustment, credit of input tax cannot be denied on this ground alone.

Ruling of AAR

Applicant can pay the consideration for inward supplies by way of setting off book debt. The GST Act and rules made there under does not restrict the recipient from claiming the input tax credit when consideration is paid through book adjustment, subject to the conditions and restrictions as may be prescribed in the manner specified in the section 16 and 49 of GST Act.

6. SHRI NAVODIT AGARWAL – AAR CHHATTISGARH (2019-TIOL-132-AAR-GST)

Facts, Issue involved and Contention of applicant

Applicant is engaged in the business of transporting cement/clinkers. Applicant entered into an oral agreement with Shree Raipur Cement (Service Recipient). In the oral agreement, Shree Raipur Cement proposed that while transporting their cement/clinkers, diesel will be provided by them to the applicant.

Applicant has sought advance ruling as to whether diesel cost in respect of transportation is to be included or excluded while charging GST on freight amount.

Applicant's submission

Applicant submitted that it has gone through valuation rules of the CGST Act. They submitted that if the service recipient provides any input goods to service providers while rendering the service, the cost of goods will be included in taxable value of services provided by the service provider and the service receiver

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needs to raise separate bill to service provider for that input goods.

Discussions by and Observations of AAR
Section 7(1)(a) of the CGST Act, 2017 defines "Supply" to include –

"(a) All forms of supply of goods or services or both such as sale, transfer, barter, exchange, license, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business;".

Section 15(2)(b) of CGST ACT, 2017 stipulates as under:-

"Any amount that the supplier is liable to pay in relation to such supply but which has been incurred by the recipient of the supply and not included in the price actually paid or payable for the goods or services or both is includible in value."

This cannot cover free inputs or services supplied by recipient, as only 'amount' paid by recipient on behalf of supplier is includible. This would be so only where there was contractual liability on supplier to make those supplies.

The authority also referred the definition of consideration u/s. 2(31) of the CGST ACT, 2017 which is stipulated as under:-

"Consideration in relation to the supply of goods or services includes:

(a) Any payment made or to be made, whether in money or otherwise, in respect of, in response to, or for the inducement of, the supply of goods or services, whether by the recipient or by any other person but shall not include any subsidy given by the Central Government or a State Government;".

In this case, diesel provided by the service recipient forms an important and integral component of this business process, without which the process of supply of cement cannot get materialised.

Service recipient i.e., M/s. Shree Raipur Cement is providing diesel to the vehicles used by the applicant to transport cement/clinker in the course of business of cement by the cement company. Diesel so provided by the service recipient to the applicant for use in trucks/vehicles of the applicant forms an important and integral component of this business process, without which the process of supply of cement can never get materialized.

Any amount that the supplier is liable to pay in relation to such supply but which has been incurred by the recipient of the supply and not included in the price actually paid or payable for the goods or services or both is includible in value.

Ruling of AAR
Applicant is required to charge GST on the total amount including the cost of diesel i.e., on the total freight inclusive of the total cost of diesel so provided by the service recipient i.e., M/s. Shree Raipur Cement.

7. M/S. RAMNATH BHIMSEN CHARITABLE TRUST – AAR CHHATTISGARH (2019-TIOL-127-AAR-GST)

Facts, Issue involved and Contention of Applicant
Shree Ramnath Bhimsen Charitable Trust is running two girls hostels. Each hostel is providing accommodation and other services to girl students, which include well-furnished residence, security, homely ambience, nutritious food, parking space etc. and in consideration, hostel is charging a nominal lump-sum fee of ₹ 6000/- per month per boarder. If any boarder want to reside in hostel for few days, the boarder is allowed to stay at nominal charge of ₹ 240/- per day.

The hostel is working as a non-profit concern (certified u/s. 12A of Income-tax Act, 1961),

as whatever consideration is charged from the boarders, the same are only for meeting the maintenance and administrative expenses for running the hostel.

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

1. *Whether the activity of providing the hostel on rent to boarder is exempted? If yes, under which exemption notification, the same is exempted?*

2. *Whether above activity is taxable? If yes, under which service access code, the same is taxable?*

Applicant's submissions

GST legislation does not define the word 'Hostel'. However, in common parlance, it means an establishment, which provides inexpensive food and lodging for a specific group of people, such as students, workers or travelers. Hostel is nothing but giving residential dwelling on rent to be used for the purpose of residence.

In present case, hostel is providing the residence to girl students solely for residential purpose and therefore, the same is fully covered under Entry No. 12 of Notification No. 12/2017-Central Tax (rate) which prescribes that services by way of renting of residential dwelling for use as residence is exempted from GST.

Applicant also considered Entry No. 14 of Notification No. 12/2017-Central Tax (Rate) dated 28th June 2017 which prescribes that services by a Hotel, Inn, guest house, club or campsite, by whatever name called, for residential or lodging purpose, having declared tariff of a unit below ₹ 1000 per day or equivalent is exempted from GST.

In view of applicant, hostel is an inn, which gives rooms on rent to girl students. Further, as the notification specifies the term 'by whatever name called' which implies that even other related services providers will be exempted even though the same is not known to be hotels, inn etc. Hostel is charging ₹ 6000 per month (i.e.. far below ₹ 1000 when computed on daily basis). Thus, hostel will not be liable to GST as per above Notification.

Discussions by and Observations of AAR

With regard to above, on observation of information submitted by the applicant it is evident that the girls residing in hostel are provided with various facilities like food supply from canteen, parking space, etc., which are all taxable supplies.

The accommodation facility at hostel is the only principal supply u/s. 2(90) of the Act and all other facilities are interrelated as these are provided exclusively to the occupants of hostel only, without any extra charge.

Authority agreed to the Circular No. 32/06/2018-GST as all taxable services provided by the Hostel are naturally bundled, therefore, covered under definition of 'Composite Supply' u/s. 2(30) of the Act.

Hostel is charging an amount of ₹ 6000 per month per child for accommodation services, which is less than ₹ 1000 per unit when computed on daily basis.

Ruling of AAR

Authority held that activity of accommodation services (being principal supply) for which the applicant is collecting amount below ₹ 1000 per day are exempt from GST under Entry No. 14 of Notification No. 12/2017-Central Tax (Rate).

❍❑❍

ML-833

CA Rajiv Luthia & CA Keval Shah

INDIRECT TAXES
Service Tax – Case Law Update

Citation: 2019-TIOL-1468-CESTAT-MUMBAI

Case: M/s. State Street Syntel Services Pvt. Ltd. vs. CCE & CT, Mumbai

Facts of the Case

The appellant is engaged in export of business auxiliary service/manpower recruitment/ supply agency services. Since the credit of service tax paid on input services used for export of services get accumulated, therefore, the appellant filed two refund claims (i) for accumulated CENVAT Credit & (ii) for Swachh Bharat Cess (SBC) for the period July, 2016 to September, 2016.

The SCN was issued to reject the refund claim of SBC alleging that it is an additional cess levied over and above service tax and is not integrated in the CENVAT chain and once this is the case, the appellant could not have availed credit in the first placed and hence, refund of such SBC does not arise.

Therefore, the appellants are with the present appeal.

Arguments Put Forth

The Appellant made the following submissions:

a) Refund of SBC is already allowed to SEZ, units *vide* Notification No. 2/2016-ST, therefore refund of the same in respect of STPI units (i.e., Non SEZ) should be allowed being export of service.

b) SBC was introduced by Section 119(5) of Chapter VI of the Finance Act, 2015, all provisions of Chapter V of Finance Act, 1994 and the rules made therein will apply including those relating to refunds and exemption from tax, interests and imposition of penalty in relation to levy and collection of SBC on taxable services and, therefore SBC is nothing but service tax and the provisions relating to refund of service tax are applicable for refund of SBC also.

c) Reliance was placed on *CCE, Belgaum vs. Shree Renuka Sugars Ltd. 2014 (302) ELT 33 (Kar) [2014-TIOL-98-HC-KAR-CX], TVS Motors Co. Ltd. vs. Union of India reported in 2015 (323) ELT 57 (Kar) [2015-TIOL-1478-HC-KAR-CX] & Ramco Cements Ltd. vs. CC, CE & ST, Bangalore reported in 2018 (362) ELT 841 (Tri. Bang) [2018-TIOL-3553-CESTAT-BANG.]*

The Respondent made the following submissions

a) SBC is the additional Cess levied over and above the refund of SBC does not arise.

Decision of the Tribunal

a) It is clear that the SBC is levied and collected for the purpose of financing and promoting Swachh Bharat initiatives or for any other purpose relating thereto but in the nature of Service Tax.

b) Issues raised *qua* Education Cess, Secondary and Higher Education Cess and, Sugar Cess, Automobile Cess etc. were settled in favour of assessee either Hon'ble Supreme Court or by the Hon'ble High Court and those were held to be tax/duty.

c) The Hon'ble Supreme Court in the matter of *Barnagore Jute Factory Co. vs. Inspector of Central Excise; 1992 (57) ELT 3 (SC) = 2002-TIOL-22-SC-CX* has laid down that levy and collection of Cess on jute manufacturer should be considered as a duty of excise when the machinery provisions of Central Excise Act and Rules were made applicable for levy and collection of jute cess.

d) A tax recovered by the Government goes into the Consolidated Fund of India which is utilised for all public purposes and no money out of the Consolidated Fund of India shall be appropriated except in accordance with law and for the purposes and in the manner provided in the Constitution. Whereas a cess or fee does not become part of the Consolidated Fund and are earmarked for the purpose of services for which it is levied. A Cess can never become part of the Consolidated Fund. It should be earmarked and set apart for the purpose for which it is levied. As per Section 119(4) *ibid* the proceeds of SBC shall first be credited to the Consolidated Fund of India.

e) SBC may be considered as separate levies from the Service Tax but the same legal framework as applied for service tax are to be applied for levy and collection of SBC since the provisions of Chapter V of the Finance Act, 1994 and the rules made thereunder are applicable to SBC

f) Therefore, SBC paid on input services has to be available as CENVAT Credit and the same can be discharged by utilising Cenvat Credit and the appellant is therefore entitle for the refund of it.

Citation: 2019-TIOL-1514-CESTAT-Chandigarh

Case: DLF Commercial Projects Corporation vs. CST, Gurgaon

Background Facts of the case

The appellant is engaged in the business of construction and development of integrated township. The statement of Assistant General Manager (Commercial & Taxation) of the appellant company recorded stated that they neither executed any sale deed nor did they pay any stamp duty to the State Government on their activity of transferring the land development rights and did not pay any service tax on the consideration received on account of transferring land development rights. Various Land-Owning Companies (LOCs) had executed Land Development Agreements or MOUs or both with appellants regarding transfer of the land development rights. The appellant's transferred these land development rights to M/s. DLF Limited and/or its associate or outside parties. It was alleged by the department & held by adjudicating authority that they have transferred development rights, therefore, they are liable to pay service tax on the said activity.

ML-835

Arguments put forth

The Appellant made the following submissions:

a) M/s. DLF Ltd gave Business Advance of ₹ 1424.83 crore to the Appellant from time-to-time for the purpose of purchase of land/development rights. The Appellant, in turn, transferred the very same amount in the nature of Refundable Performance Deposit to various LOC's to enable them to purchase land. It was the responsibility of the Appellant to obtain/ arrange license from the Government of Haryana for the purpose of developing the land located in the State of Haryana.

b) The various clauses of "Business Development Agreement" dated 2-8-2006 between DLF Ltd. and Appellant clearly says that the Appellant shall, in future, transfer the development rights and does not say that the Appellant has actually transferred the development rights. The Agreement is futuristic in nature.

c) The LOC's have certified that the "Refundable Performance Deposit" remitted to them is not a consideration towards transfer of "Development Rights. The "Performance Deposit" shall be refundable in future as and when either the sale deed is executed for the land or agreement is executed for transfer of "Development Rights".

d) The Annual Accounts of the Appellant does not say that the development rights have been transferred by the Appellant to M/s. DLF Limited. In addition, independent CA *vide* Certificate dated 30-4-2018 certified that the Appellant neither purchased the land nor purchased the "Development Rights".

e) Nevertheless, the impugned transaction in relation to immovable property which is excluded from the definition of "service" u/s. 65B(44) of the Act. The definition of "immovable property" as per General Clauses Act, includes not only "land" but also the benefits "arising out of land. TDR is a benefit arising out of land so as to fall under "immoveable property, as held by *Sadoday Builders (P) Ltd. vs. Jt. Charity MANU/MH/07912011* & *Chheda Housing Development Corpn vs. Bibijan Shaikh 2007 (2) Bom CR 587.*

f) The authorisation given to a "Developer" to develop the land and sell super-structure in perpetuity shall undisputedly fall within the words "benefit arising out of the land" and shall, therefore, be held to be "immovable property". Consequently, no "Service Tax" shall be payable under Section 66.

g) In the instant case, the land-owning company transfers land development rights to the developers, the developers get the right to not only to develop project on such land but also the right to sell such developed property along with undivided interest in the land underneath and to receive payments for such transfers from the buyers. It is the ownership of the land, which stands transferred effectively by the land-owning company in return of consideration payable by the developers. The moment it is either land or "benefits arise out of land", it goes outside the purview of "Service" as defined in Section 65B(44) of Finance Act, 1994.

h) It is submitted that it is not only the possession, which stood transferred with the right to use, enjoy and construct building/super structure, but, at the same time, undivided right, title and interest in the land also stand transferred under the Deed of Conveyance on which stamp duty has been paid and the Deed of Conveyance has been registered before the Sub-Registrar.

ML-836

i) Further, in the last five years, repeatedly, various Trade Forums including Confederation of Real Estate Developers Association of India, Northern Region, sent a representation to the Government seeking clarification/confirmation about the levy of "Service Tax" on "Development Right" and the Government never, in the past, viewed that the Service Tax is at all payable. Hence, extended period cannot be invoked.

The Respondent made the following submissions

a) The two transactions which are independent and mutually exclusive should not be confused as one transaction. Based on above it is submitted that the two transactions of transfer of development rights viz. "between various land owners and appellant and " between appellant and M/s. DLF " are, mutually exclusive, independent but separately taxable transactions and should not be confused as one. Further, in the present Appeals it is not only the transactions between appellant & M/s. DLF which is under dispute and hence only the taxability of same should be adjudicated.

b) It is relevant to refer the note given in the above annual financial statement which explains that "The advances given by the firm to the LOCs in pursuance of the development agreements entered into with them, are classified as inventory where the LOC has confirmed that it has either already acquired the land or is in an advance stage of acquiring the same as on the balance sheet date. All other advances are classified as loan Advances.

Decision

a) It is a fact on record that the land owning company remained the owner of the land and have not transferred the land in the name of the appellant unless and until if the appellant become the owner of land, how the appellant can transferred development right in favour of the DLF Ltd. it is mere transaction of the sale and purchase of land or purchase of land by the appellant for DLF Ltd., for further development

b) The activity of the appellant would have been started only after acquisition of land and thereafter to procure NOC from the various Govt. Authorities and thereafter development activities on the land.

c) When the land-owning company transfers land development rights to the developers, the developers get the right to not only to develop project on such land but also the right to sell such developed property along with undivided interest in the land underneath and to receive payments for such transfers from the buyers. Thus, it is the ownership of the land, which stands transferred effectively by the land-owning company in return of consideration payable by the developers. The moment it is either land or "benefits arise out of land", it goes outside the purview of "Service" as defined in Section 65B(44) of Finance Act, 1994.

d) Reliance is placed on decision of *Premium Real Estate Developers vs. CST-Service Tax, Delhi in Appeal No. ST/50103-50104/2014 = 2019-TIOL-725-CESTAT-DEL*, where the tribunal in similar facts held that since the specific remuneration has not been fixed in the deal for acquisition of the land we are of the view that both the parties have worked more as a partner in the deal rather than as an agent and the principle, therefore we are of view that taxable value itself has not acquired finality in this case.

e) As regarding the legal aspect of applicability of service tax on TDS, we rely on the decision of Hon'ble High Court which observed in the case of Sadoday Builders Private Ltd. and Ors. (supra) that transferrable development right is immovable property. Therefore, out of the purview of definition of term "service".

f) In the instant case, we hold that the activity in question which is only acquisition of land, therefore, no service tax is payable by the appellant in terms of Section 65B(44) of the Finance Act.

Citation: 2019-VIL-233-DEL-ST-WP

Case: Amendus India Private Limited vs. Principal Commissioner CE & ST,

Background facts of the case

The Petitioner provides, *inter alia*, computer data processing software, which is used by travel agents and ticket booking entities in the Airline industry. The Anti-evasion unit of service tax undertook search of the registered premises in the year 2016 and various documents were submitted before the investigating authorities. After 2 years, fresh summons was issued in the year seeking for various information, which were submitted by the Petitioners immediately.

Thereafter SCN was issued on 4th September 2018 for a quantum of ₹ 99,45,64,411/- plus interest and penalty u/s. 76. The Petitioners drew attention of the authorities for pre-consultation of SCN in view of Master Circular dated 10th March, 2017 read with an instruction dated 21st December, 2015 issued by the CBEC. Since no response was received, the Petitioner filed the current writ petition.

The question that arose in the present writ petition is whether prior to issuing the impugned SCN, the Office of the Principal Commissioner, ought to have held a pre-notice consultation with the Petitioner in terms of para 5.0 of 'Master Circular' dated 10th March, 2017 issued by the CBEC.

Arguments put forth

The Appellants submitted as under:

a) The first report of the Tax Administration Reform Commission (TARC) made a recommendation as under:

It is desirable to avoid disputes where a corroborative approach can provide a solution. An administrative pre-dispute consultation mechanism may be instituted in both the organisations for resolving tax disputes at the pre-notice stage through an open dialogue with the taxpayer, in which both sides articulate and discuss their respective positions and views on the matter at hand. An amicable resolution would be possible when a common view emerges on the facts and the legal position. It is expected that this process, if followed in proper spirit, would lead to elimination of a large number of disputes leaving only a few contentious matters in which mutual agreement is not reached. Such disputes would follow other legal channels.

b) These recommendations were accepted by CBEC and issued a Master Circular on 10th March 2017 which mandated a pre-consultation of SCN for issues having a demand in excess of ₹ 50 lakhs.

c) The mandatory character of the Master Circular can be traced to Section 83 of the Finance Act, 1994 which makes Section 37B of the CE Act, 1944 applicable in relation to service tax. In terms Section 37B instructions issued by CBEC would be binding on the Department

The Respondents submitted as under:

a) There are two exceptions carved out for the Respondent to engage in a

pre-SCN consultation as stated in the Master Circular. The first is that the SCN is preventive and the second is that it is related to an offence in terms of the Finance Act, 1994.

b) Since the SCN was preceded by a search that was conducted in the business premises of the Petitioner, and the Petitioner also rendered itself liable for penal action 'for suppression of facts and contravention of various statutory provisions with intent to evade payment of due service tax' and other incidental levies, the SCN partakes character of an 'offence related' SCN and therefore falls within the exceptions carved out under para 5.0 of the Master Circular.

c) Respondents stated that there was no noting in the file to check whether any decision was taken whether pre-consultation should be provided or not.

Decision

a) Since there is no noting in the file on providing of pre-consultation of SCN, it appears that the Respondent completely ignored the Master Circular before proceeding to issue the impugned SCN.

b) The above submission made by the Respondents runs contrary to the very object of para 5.0 which is to narrow down the scope of the dispute by engaging the Assessee on specific areas where the Respondent may require information/clarification from the Assessee regarding alleged evasion of service tax. In the context of the present case, in relation to documents recovered during the search and statements recorded of representatives to the Petitioner in that process, several questions may have arisen for consideration by the Respondent which may require a clarification from the Petitioner as to its conduct. It is to facilitate this very exercise that para 5.0 finds place in the Master Circular. The mere possibility that at the end of the adjudication process, the Petitioner may have to face consequences for having committed an 'offence' under Finance Act, 1994 need not *per se* render the SCN itself as an 'offence related' SCN. If that were to be the logic, then in every case para 5.0 can be dispensed with on the ground that the adjudication of the SCN is likely to be led to the noticee facing proceedings for having committed an offence. The exception would then become the rule and not *vice versa*, and the need for any pre-notice consultation being rendered redundant. Further, without the conclusion of the adjudication on the SCN, the Respondent would not be in a position to decide whether an offence is made out.

c) In the present case, the Court was satisfied that it was necessary in terms of para 5.0 of the Master Circular for the Respondent to have engaged with the Petitioner in a pre SCN consultation, particularly, since in the considered view of the Court neither of the exceptions specified in para 5.0 were attracted in the present case.

Accordingly, the SCN was set aside by the Court and directed the Respondents to fix an appointment for providing a pre-consultation.

Citation: 2019-VIL-282-CESTAT-BLR- ST

Case: Carl Bechem Lubricants India Private Limited vs. CCE Bengaluru West

Background Facts of the case:

The Appellants are engaged in the manufacture of Industrial Special Lubricating Creases falling under Chapter Sub-heading 27 and 34 of CE Tariff Act, 1984 and are availing the CENVAT

credit on input, capital goods and input services under the CCR, 2004.

During the course of audit, it was observed that the appellants have revenue from sales exports trading. On verification of the details, it was seen that appellants import certain materials from Germany and Japan and the same are bonded in their Customs Bonded Warehouse in their premises at Chennai and the same are exported to their Trading Partners in Sri Lanka *viz.*, M/s. Monara Engineering & Trading Pvt. Ltd. for further supply to their customers at Sri Lanka. The appellants had entered into an agreement with M/s. Monara Engineering & Trading Pvt. Ltd. for trading of goods to Sri Lanka and as per Clause 16(k) of the said agreement, if the appellants, due to some unavoidable reasons and in consideration with their Trading Partner, may supply their goods directly to the customers. In such cases, on mutually agreed terms, the Trading Partner will be compensated with ORC – Over Riding Commission for such transactions. The department entertained the view that the appellants are not entitled to CENVAT credit and they have irregularly availed the CENVAT credit. Thereafter, a SCN was issued proposing to demand ₹ 3,47,999/- being the irregularly availed service tax input credit on the overriding commission.

Arguments put forth

The assessee as Appellants submitted as under:

a) The eligibility of CENVAT should be determined in the light of the Export Policy of the GOI and not independently under CCR. In the present case, appellant has received services from an overseas partner and has paid the service tax under RCM u/s. 66A. If the CENVAT credit is denied to the appellant, then the appellant shall be entitled to rebate of the service tax paid in terms of Notification No. 41/2012-ST dated 29-6-2012.

b) Any benefit from an exemption Notification can be availed at the appellate stage as well and the Department cannot deny any benefit arising out of the substantial entitlement based on procedural lapses. They relied on decision of *Monarch Catalyst Pvt. Ltd. vs. CCE: 2016 (41) STR 904* wherein it was held that assessee was entitled either to claim refund of service tax used in relation to export of goods under Notification No. 41/2007-ST or avail credit of service tax paid on such input services. It was held that credit was not deniable to the assessee choosing to avail it and not claiming refund of service tax under the said Notification.

c) Appellants relied upon the decision of *Cap & Seal (Indore) Pvt. Ltd. vs. CCE: 2018 (15) GSTL 74 (Tri.-Del.)* wherein it has been held that there is only trading activity in terms of Finance Act, 1994 and not trading service and on export of goods, assessee is entitled to refund of service tax paid on services availed for export and it is a revenue neutral situation.

d) Appellants also relied upon the decision of *Jotindra Steel & Tubes Ltd. vs. CCE, Delhi: 2014 (36) STR 672 (Tri.-Del.)* wherein it was held that when two options are available, the assessee has choice to avail any one of such option. Further, Notification which permits refunds does not debar availment of credit in case refund is not claimed. He also submitted that it is a settled principle of law that it is an option for the assessee either avail exemption or forgo the same in order to avail credit. For this submission, he relied upon the decision in the case of *CCE, Vadodara vs. Narmada Chematur Pharmaceuticals Ltd.: 2005 (179) ELT 276 (SC)* wherein the Hon'ble SC in similar circumstances

held that when an assessee does not avail an exemption in order to take credit and when such credit is subsequently held to be wrongly availed, which is exactly equivalent to the amount of duty paid by not availing the exemption, the consequence is revenue neutral and hence, demand for such wrong availment of credit is not sustainable. Learned counsel also submitted that extended period of limitation will not be invokable, in the instant case, since the issue is entirely revenue neutral and adequate disclosures were made in the balance sheet of the appellant.

The Respondent submitted as under:

a) The learned AR defended the impugned order and submitted that the appellant has irregularly availed the CENVAT credit of service tax paid under Section 66A of the Finance Act on the commission paid to M/s. Monara Engineering & Trading Pvt. Ltd., Sri Lanka for export of trading goods. He further submitted that in terms of Rule 2(l) of the CCR, 2004, CENVAT credit availed exclusively on trading activity is not admissible as the same does not come under either the purview of manufacture or provision of taxable service.

Decision

a) In the present case, it is not disputed that the appellant has in fact received services of overseas trading partner and the same has been used for export of goods. It is also a fact that appellant has actually paid the service tax as applicable under RCM u/s. 66A. Further, the appellant has not sought refund or exemption from payment of service tax under any other provisions or Notification and has taken CENVAT credit of the service tax paid.

b) Further, it was held that such availment of CENVAT credit of service tax paid on commission should be allowed under CENVAT Credit Rules in view of the Export Policy of Government. Further, the decisions relied upon by the appellant cited supra mainly the decisions in the cases of Monarch Catalyst Pvt. Ltd. and Jotindra Steel & Tubes Ltd. are squarely applicable to the facts of this case. By following the ratio of the above said decisions, the Bench was of the considered view that the impugned order is not sustainable in law.

Accordingly, the appeal filed by the Appellants was allowed.

Citation: 2019-VIL-302-CESTAT-CHE-ST

Case: Bharat Cylinders vs. CCE, Madurai

Background facts of the case

Appellants were *inter alia* rendering services of segregation, reconditioning, surface cleaning and washing of empty cylinders meant for LPG cylinders which, according to department, was exigible to service tax liability under the category Management, Maintenance and Repair Services (MMRS).

Arguments put forth

The Appellants submitted as under:

a) The repair of valve leakage during the process of testing are covered under Management, Maintenance or Repair Services (MMRS) attracting service tax as per the impugned order. They have been engaged in the statutory testing of LPG Cylinders under Gas Cylinder Rules, 2004 and the Indian Explosives Act, 1884. The cylinders are to be tested periodically and a certificate was required to be issued to the effect that the cylinders had undergone various tests. The impugned

activity therefore cannot be classifiable under MMRS.

b) Reliance was placed on the decisions of *Harshita Handling vs. CCE, Bhopal, 2010 (19) STR 596*, wherein it was held that the activities of the appellants would not get covered under "Technical testing and certificate service or Management, Maintenance and Repairs service".

c) Alternatively, the appellants submit that they are entitled for benefit of notification No. 12/2003 which exempts the value of goods involved in taxable service. As per the Notification, the value of goods and materials sold by the service provider to the recipient are excluded from the payment of service tax, if there is sufficient evidence for the value of the goods sold separately. In this connection, the appellant submits that they have purchase bills to show that the paints purchased have suffered VAT and the appellants also paid appropriate VAT on such value of sale of paint. They rely on the ratio of the Tribunal decision of *Mehta Plast Corporation vs. CCE, Jaipur – 2012-TIOL-616-CESTAT.*

The Respondents submitted as under:

a) The Ld. Counsel appearing on behalf of the Respondents relied on the reasoning provided in the Order of Commissioner Appeals.

Decision

a) The testing of LPG cylinders, under a Statute, is no doubt a statutory obligation, but the appellant is a private organisation and its appointment by statutory notification is not there. Thus, the appellant is only carrying out an outsourced job and in the absence of any document as to the statutory notification appointing it, we are unable to accept the appellant's arguments. When tax payment is a statutory obligation, each taxpayer cannot claim that his/its activities to be exempt because of his/its discharge of statutory obligation. It may be a duty cast on each tax payer, but the same cannot be equated to be an exempted activity. For the above reasons we do not accede to the appellant's contentions that it is carrying out a statutory obligation and hence, its services are exempt. Further, the appellant has claimed that the cylinders are being delivered after testing, in their own vehicles as agreed to in terms of a contract. This agreement is an *inter se* agreement between the appellant and the other person/agency, which is binding only on the parties to the said agreement and therefore, it can never have any implications on the appellant's statutory obligations nor could it be even imagined to have any effect on any other person.

Accordingly, the appeal was not allowed in terms of the demand raised in the SCN.

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> No man is to be judged by the mere nature of his duties, but all should be judged by the manner and the spirit in which they perform them.
>
> — *Swami Vivekananda*

Janak C. Pandya *Company Secretary*

CORPORATE LAWS

Company Law Update

Case Law # 1

[2019] 214 Comp Cas 59 (Delhi)

[In the Delhi High Court]

(1) Cushman and Wakefield India P. Ltd.

(2) Knight Frank (India) P. Ltd.

(3) CBRE South Asia P. Ltd.

(4) Jones Lang Lasalle Property Consultants (India) P. Ltd. v. Union of India and Another

The valuations by the registered valuer under section 247 and Rules made thereunder of the Companies Act, 2013 ("Act") is to develop it as a "Profession" and not as a "Business" and thus every effort has been made to avoid situation of conflict of interest.

Brief

The 4 writ petitions were filed by four different petitioners having a common issue.

1. Ministry of Company Affairs has notified the Companies (Registered Valuers and Valuations) Rules, 2017 ("Rules") under section 247 of the Act.
2. The Rule 3 (2) of the Rules provides that - No partnership entity or company (which also includes its subsidiary, joint venture or associates or another company or body corporate) shall be eligible to be a registered valuer, if it has been set up for objects other than for rendering professional or financial services including valuation services.
3. The petitioners are engaged in the real estate consultancy business which also includes providing real estate valuation services.
4. Petitioners are the subsidiary of a reputed body corporate and universally recognised as a lauded leader in providing valuation services.
5. Petitioners have a rich and varied experience in the field of valuation and are better equipped as opposed to an individual valuer.
6. The above rule affects the investment/acquisition of assets in India as both Indian and foreign investors rely on globally recognised valuation service providers.

7. The Constitution of India has guaranteed the right to carry on trade and business, which is impaired by the above Rules.

8. The above rule imposes unreasonable restrictions on the petitioner's right to carry on trade and business.

9. Petitioners are not only discriminated against individuals and partnership entity but also such companies which are not a subsidiary, joint ventures or associates of other companies'/body corporates.

10. Thus, the above Rules are unconstitutional for violating Article 14, Article 19(1)(g) and Article 301 of the Constitution of India.

11. In their support, the petitioners relied upon the Hon. Supreme Court Judgment in the case of *Cellular Operators Association of India vs. Telecom Regulatory Authority of India [2016] 7 SCC 703.*

The petitioners prayed to the Hon. High Court to issue appropriate writ, order and/or direction declaring the Rule 3(2) of the Rules unconstitutional for violating Article 14, Article 19(1)(g) and Article 301 of the Constitution of India.

From Government side, following submissions are made.

1. The Rules are self-contained code for the purpose of valuation of any properties/ stocks, shares, debentures, securities or goodwill or any other assets on net worth of a company.

2. The explanation to Rule 1(3) stipulates that the conduct of valuation under any other law other than under the Act shall not be affected.

3. The new section 247 of the Act introduced for the first time the concept of valuation by a registered valuer having qualifications and requisite experience so that an impartial, true and fair valuation may be made.

4. Until the provisions of valuation in the Act and Rule, there has not been any generally accepted and uniform standards in asset valuation system in India.

5. In absence of uniform standards, asset valuation in India was not considered credibly.

6. The reference to provisions under the Act and under the Insolvency and Bankruptcy Code 2016, where the valuation required was made.

7. Due to importance of valuation, every effort has been made to avoid situation of conflict of interest. The idea is to develop the valuation as a "Profession" and not as a "Business".

8. The registered valuer is required to pass an exam for which syllabus, format and frequency of the valuation examination have been prescribed.

9. There is a rational nexus to the object of disqualifying all entities with interest in other professions or business/enterprises to maintain integrity of the profession and avoid conflict of interest.

10. In support for the above submission, the Supreme Court judgment in the case of *Dr. Haniraj L. Chulani vs. Bar Council of Maharashtra and Goa [1996] 3 SCC 342* and latest Supreme Court Judgement in the case of *Swiss Ribbons P. Ltd vs. Union of India [2019] 213 Comp Cas 198 (SC)* in writ Petition (Civil) No. 99 of 2018 on challenging the provisions of IBC were referred.

Judgment

The Court dismissed the petitions on the following grounds.

1. The relevance of the Supreme Court case in re *Dr. Haniraj L. Chulani vs. Bar Council of Maharashtra and Goa* in this case was accepted with the observation made as follows.

    a. The Supreme Court has said that … in view to ensuring that only profession-oriented and service-oriented people to join the Bar and that no so oriented are kept out.

    b. While under Article 19 (1)(g), all citizens have a right to practice any profession or to carry any occupation, trade or business it is not the absolute right and that the same is subject to sub-article (6). As per the said sub-article (6), state may impose reasonable restrictions in the interest of the general public.

    c. With regards to Article 14, the rule is not unreasonable, arbitrary or capricious from any angle as on same ground as article 19(1)(g) for imposing a reasonable restriction.

2. The object and intention behind rule is clearly to introduce higher standards of professionalism in valuation industries and to obviate the possibility of conflict of interest on account of divergent interest of constituent/associates entities specifically for the purpose of the Act and IBC.

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HOT OFF THE PRESS!

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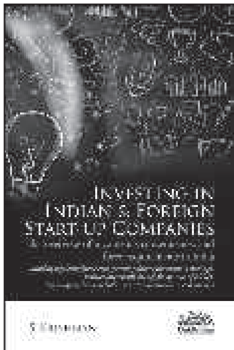

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S Krishnan

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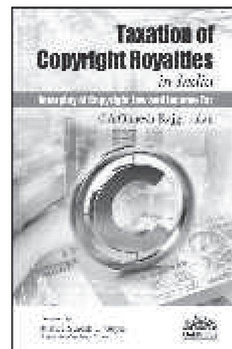
TAXATION OF COPYRIGHT ROYALTIES IN INDIA



Interplay of Copyright Law and Income Tax

CA Ganesh Rajgopalan

Foreword by
Justice Suresh C Gupte
Judge, Bombay High Court

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OTHER LAWS

FEMA – Update and Analysis

In this article, we have discussed recent amendments to FEMA through Circulars and FAQs issued by RBI. In addition to it we have discussed few recent compounding orders issued by RBI.

A. Amendment to FEMA through A.P. Dir Circular issued by RBI

I) 'Voluntary Retention Route' (VRR) for Foreign Portfolio Investors (FPIs) investment in debt

RBI based on the feedback received, RBI has revised A.P. Dir Series Circular No. 21- 'Voluntary Retention Route' (VRR) for Foreign Portfolio Investors (FPIs) investment in debt dated 1-3-2019. The changes made by the RBI are as follows:

1. Introduction of separate category *viz*., VRR Combined in Para 2(x) of the Annex. 'VRR-Combined' shall mean Voluntary Retention Route for FPI investment in instruments eligible under both VRR-Govt and VRR-Corp.

2. The requirement to invest at least 25% of the Committed Portfolio Size within one month of allotment has been removed. Earlier, successful allottees were required to invest 25% of their committed portfolio size within one month and the remaining amount within three months from the date of allotment under **para 6.a** of the A.P. Dir Series Circular No. 21 dated 1-3-2019. RBI has now amended the above direction and accordingly, amended Para 6.a provides that Successful allottees shall invest at least 75% of their CPS within three months from the date of allotment.

3. FPI are provided with an additional option at the end of the retention period to continue to hold their investment until the date of maturity or the date of sale, whichever is earlier.

   Earlier, as per the **para 6.c** of the A.P. Dir Series Circular No. 21 dated 1-3-2019, in case if FPI decides not to continue under VRR at the end of the retention period, FPI may liquidate its portfolio and exit, or it may shift its investments to the 'General Investment Limit'.

   Under the revised direction, FPI has the option to continue to hold their investment until the date of maturity or the date of sale whichever is earlier. **Para 6.c** as amended now reads as follows:

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Para 6.c: In case an FPI decides not to continue under VRR at the end of the retention period, it may: (a) liquidate its portfolio and exit, or (b) shift its investments to the 'General Investment Limit', subject to availability of limit under the 'General Investment Limit', or (c) hold its investments until its date of maturity or until it is sold, whichever is earlier.

Source: A.P. Dir. Series Circular No. 34 dated May 24, 2019.

(Comments: This is a welcome move which provides flexible investment option to FPIs.)

B. Updated through FAQs

I) Overseas Direct Investment

RBI update on FAQs on Overseas Direct Investment as on May 29, 2019 contains the following change:

1) Answer to Question 62 has been re-drafted

Q.62. Is development/construction (and thereafter, sale) of residential/ commercial premises by an overseas Joint Venture (JV) or Wholly Owned Subsidiary (WOS) treated as real estate business under ODI regulations (FEMA Notification No. FEMA 120/RB-2004 dated July 7, 2004 as amended from time-to -time)?

Ans: No. In terms of Regulation 5(2) read with Regulation 2(p) of Notification No. FEMA 120/RB-2004 dated July 7, 2004, as amended from time-to-time, buying land (along with building/pre-existing structures) for construction/development of residential/commercial premises (before selling) as one integrated core activity, is not treated as real estate business activity.

II) External Commercial Borrowings (ECB) and Trade Credits

RBI update on FAQs on External Commercial Borrowings (ECB) and Trade Credits as on May 29, 2019 has been amended entirely to align with the revised FEMA Notification No. 3(R)/2018-RB dated 17-12-2018.

You are requested to refer the same at: https://www.rbi.org.in/scripts/FS_FAQs.aspx?Id=120&fn=5.

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)

Delay in reporting the transfer of shares by Resident to Non-Resident.

Applicant	M/s. Quiver Digital Solutions India Private Limited
Compounding Application Number	C.A. BGL 330/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under Compounding Order	₹ 26,683/-

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Date of order	2nd April, 2019
Facts of the case	Delay in reporting of foreign remittances, delay in submission of Form FC-GPR & delay in reporting transfer of shares in Form FC-TRS beyond the stipulated time period.
Contravention	Contravention of Paragraph 9(1)(A) of Schedule I to Notification No. FEMA 20/2000-RB, due to delay in reporting of foreign inward remittances Contravention of Paragraph 9(1)(B) of Schedule I to Notification No. FEMA 20/2000-RB, due to delay in submission of Form FC-GPR Contravention of Regulation 10A (b) (i) read with Paragraph 10 of Schedule I to FEMA 20/2000-RB, due to delay in reporting of transfer of shares.
Comments	Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations; Regulation 13.4 of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Regulation paragraph 10 of schedule 1 of erstwhile FEMA 20/2000-RB dated May 3, 2000.

2) Foreign Exchange Management Deposit Regulation (FEMA 5/2000-RB dated 3-5-2000)

Transfer of funds from NRE account to Ordinary Savings Account

Applicant	Mr. Thakorbhai Dahyabhai Patel
Compounding Application Number	C.A. No. 85/2019
Compounding Authority Name	Foreign Exchange Department, New Delhi
Amount imposed under Compounding Order	₹ 1,13,758/-
Date of order	18th March, 2019
Facts of the case	The applicant is an OCI and a person non-resident in India in terms of Section 2(w) of Foreign Exchange Management Act, 1999. The applicant had opened and maintained ordinary saving bank account with ICICI Bank Ltd. and Prime Co-operative Bank Limited.

	The applicant had granted a loan of to his friend Mr. Narendra V. Solanki, a person resident in India, from his ordinary savings account maintained with ICICI Bank. The amount represented either transfer of funds from his NRE Account maintained with HDFC Bank or amount received from LIC on his father's death. The applicant had transferred ₹ 85,01,100/- from his NRE account to his ordinary saving account. Transfer of funds from NRE account to ordinary savings account: Regulation 4(c) of Schedule 1 to Notification No. FEMA.5/2000-RB dated 3rd May 2000 states that "permissible debit of NRE account is transfer to NRE/FCNR (B) accounts of the account holder or any other person eligible to maintain such account." In this case, since the applicant had transferred the amount from his NRE account to his ordinary resident account which is not the permissible mode of debit to the NRE account. Therefore, applicant had contravened the provision of regulation 4(c) of FEMA notification *ibid*.
Contravention	Foreign Exchange Management (Deposit) Regulations, 2000 has been replaced by revised regulations; Regulation 4(c) of Schedule 1 of extant FEMA 5(R)/2016-RB dated 4-4-2016 corresponds to Regulation 4(c) of Schedule 1 of erstwhile FEMA 5/2000-RB dated 3-5-2000.

3) Acquisition and transfer of Immovable Property in India (FEMA 21/2000-RB)

Acquisition of Immovable property (agricultural land) in India by a NRI without the RBI permission

Applicant	Mr. Chandan Kumar Mishra
Compounding Application Number	C.A. No. 89/2019
Compounding Authority Name	Foreign Exchange Department, New Delhi
Amount imposed under Compounding Order	₹ 1,43,680/-
Date of order	18th March, 2019
Facts of the case	The applicant is an NRI, presently residing in California, USA.

	The applicant had purchased the immovable property *viz.*, 8 acres of agricultural land in Coimbatore, India on 21st December, 2016. Cost of Acquisition of the said property was ₹ 97,60,000/-. The total consideration has been paid to Mr. Albert Selvam towards the purchase of above mentioned agricultural land. However, all transactions have been originated from the account of Smt. Renu Devi, maintained with SBI, Salem Branch, Tamil Nadu and credited to the account of Mr. S. S. Albert Selvam. No trace of foreign inward remittance had been noticed from the account statement of Smt. Renu Devi. Hence, matter was sent to the Directorate of Enforcement, Chennai for further investigation. DOE had *vide* its letter stated no objection to the compounding application. Thus, the applicant was advised to sell the immovable property to a person resident citizen of India within six months and not to repatriate sale proceeds of the property without prior approval of the RBI subject to compounding of contravention. However, the applicant transferred the property under reference by way of gift to Mrs. Shanti Mishra, a resident citizen of India *vide* settlement deed executed on March 22, 2018. Value of land as per the valuation report submitted by the applicant appreciated to ₹ 98,00,000/-, by virtue of which applicant earned ₹ 40,000/- as undue gain.
Contravention	***Acquisition of agricultural land in India by NRI without the RBI permission***: Regulation 8 of Notification No. FEMA-21/2000-RB dated May 03, 2000 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, since the applicant being an NRI had acquired the agricultural land India without the prior RBI approval thereby contravening provision of regulation 8 of Notification No. FEMA 21/2000-RB dated May 3, 2000.
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)/2017-RB dated 26-3-2018 corresponds to Regulation 8 of erstwhile FEMA 21/2000-RB dated 3-5-2000.

	As per Master Direction on Compounding of Contravention under FEMA, if it is established that the contravenor has made undue gains, the amount thereof may be neutralized to a reasonable extent by adding the same to the calculation of compounding amount. In this case, RBI has correctly neutralized the undue gain as per the provision laid down in the aforesaid Master Direction.

4) Section 5 of Foreign Exchange Management Act, 1999 read with Master Direction on Liberalised Remittance Scheme

Gift by person resident in India to another person resident in India under the LRS route

Applicant	Shri Vinit Beriwala
Compounding Application Number	C.A. No. 4813/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under Compounding Order	₹ 96,433/-
Date of order	25th April, 2019
Facts of the case	The applicant, a resident individual remitted ₹ 61,91,076/- under the LRS route, to the overseas joint foreign currency account of his parents. Both, the applicant and his parents were resident in India.
Contravention	Section 5 of FEMA, 1999 permits a person to sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction. Further, Para 7(b) of Master Direction on LRS states that any resident individual may remit up-to USD 2,50,000 in one FY as gift to a person residing outside India or as donation to an organization outside India. In this case, since the applicant being a person resident in India had remitted an amount as a gift to his parents who were resident in India under the LRS route thereby contravening provision of Section 5 of FEMA, 1999 read with Para 7(b) of Master Direction on LRS as then applicable.

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CA Prashant Daftary & CA Samir Parmar

In Focus – Accounting and Auditing

New Audit Report - Comprehensive but Lengthy Analysis - SA 700 and SA 720

With changing times and reducing attention span of the readers it was a necessity to review the form and content of the audit report. The audit report caters to a number of users and these include educated/highly sophisticated investors and also retail investors who may have a limited understanding of regulatory requirements etc. Audit report is an important element of the audit process which communicates the audit opinion to a wide range of users and it is important that its utility to the user is of the highest value.

The Institute of Chartered Accountants of India (ICAI) has been on a constant endeavour to upgrade the auditing standards and benchmark them with the global standards. The new changes have transformed and upgraded the audit report to global standards.

In light of this a number of auditing standards have been revised in line with the global standards.

Standards	*Key Change*	*Effective date*
SA 700 (revised) Form an opinion on financial statements	New structure of audit report	1st April 2018
SA 701 Communicating key audit matters in independent auditor's report	New standard which deals with auditor's responsibility to communicate key audit matters	1st April 2018
SA 705 Modifications to the opinion in independent auditor's report	Revised to clarify the impact of new reporting requirements pursuant to changes in SA 700 and introduction of 701	1st April 2018

Standards	*Key Change*	*Effective date*
SA 706 Emphasis of matters paragraph and other matters paragraph in independent auditors report	Revised to clarify the impact of new reporting requirements pursuant to changes in SA 700 and introduction of 701	1st April 2018
SA 260 (revised) Communication with those charged with governance	Revised mainly due to introduction of standard on key audit matters. Also there are other changes in standards like communicating the use of experts by the auditor etc.	1st April 2017/ Changes related to KAM are effective from 1st April 2018
SA 570 (revised) Going Concern	Requires a separate section to be included in the auditor's report when the auditor concludes that a material uncertainty related to going concern exists and it has been adequately disclosed in the financial statements	1st April 2017
SA 720 (revised) The auditor's responsibility relating to other information	New reporting requirement relating to other information in financial statements	1st April 2018

Further consequential changes have also been made to SA 210, 220, 230, 510, 540, 600 and 710.

In this articles we focus on the analysis of two auditing standards which have been revised

- Standard on Auditing – SA 700 (revised)
- Standard on Auditing – SA 720 (revised)

Key changes

- ***Start with the audit opinion*** – Earlier the audit opinion was mentioned after auditor's responsibility para and hence was getting lost in the middle of a lot of technical literature about management responsibility, auditor's responsibility etc. This change will be very useful for the investor as they need not read the full report to understand the auditor's opinion. This is all the more relevant considering the reducing attention span of the readers of the audit report.
- ***Clarity in terms on management responsibility and auditor's responsibility on going concern*** – With rising number of companies filing for insolvency proceedings under insolvency code. This para is of paramount importance to the auditors as well as the investors for their understanding of the responsibility of the management and the auditors.
- ***Affirmative statement on other matters in annual report*** – This is an important change which is brought about by SA 720 (revised) and would ensure that auditors carefully read the other aspects of the annual report and comment in case there is any misstatement or contradiction in the items other than financial statements which are also part of the annual report.

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Benefits from readers/investors perspective

- *Transparency* - The audit opinions would no longer be binary opinion of yes or no. The new format provides the reader to understand the journey of the audit including the materiality level used, key audit issues and how they were dealt with by the auditors. This would provide the readers an insight about the entire process and thereby making it more transparent.
- *Comfort on consistency of information in annual report* – The very fact that the auditors have to comment on the other matters dealt with in the annual report provides a comfort to the readers about the overall consistency between the annual report and financial statements.
- *Effectiveness of the audit reports* – The new design of audit report is aimed at making the report more effective and self-explanatory. The changes have been made present considering the evolving legal requirement, economic environment, and needs of the users to ensure that audit reports remain effective and relevant from the investor's perspective.

We now analyse both these revised standards in detail:

(SA) 700 (Revised) Forming an opinion and Reporting on Financial statements

A. Overview and applicability

SA 700 (revised) deals with the auditor's responsibility to form an opinion on the audited financial statements and content of the audit report. It gives the fundamental principles and guidelines of reporting.

SA 700 (revised) is effective for audits of financial statements for the period beginning on or after 1st April 2018. This revised SA is not applicable to audit report signed after 1st April 2018 pertaining to financial statements for periods beginning before 1st April 2018.

This SA applies to an audit of a complete set of general purpose financial statements. General purpose financial statements are those that are prepared in accordance with a 'general purpose financial reporting framework', which is a framework designed to meet the common financial information needs of a wide range of users. This SA applies to audits of complete set of 'financial statements'.

There are other SAs which give detailed guidance on the elements of the audit report e.g., reporting of key audit matters, other information, emphasis of matter & other matters and modified opinion.

ICAI has also issued Implementation Guide for SA 700 (revised) Implementation guide has addressed certain key issues in question answer format.

Reports under different types of engagement

- When financial statements are prepared in accordance with a special purpose framework and in an audit of a single financial statement or of a specific element, account or item of a financial statement; though the reporting principles and structure is based on SA 700 (revised), there are separate SAs for guidance on issue of reporting under such circumstances. It states that auditor shall apply the requirements in SA 700 (revised), adapted as necessary in the circumstances of the engagement.
- Reporting format for report on internal financial control (IFC) over financial reporting also is derived based on SA 700 (revised). Since the illustration as per guidance note on IFC has not been

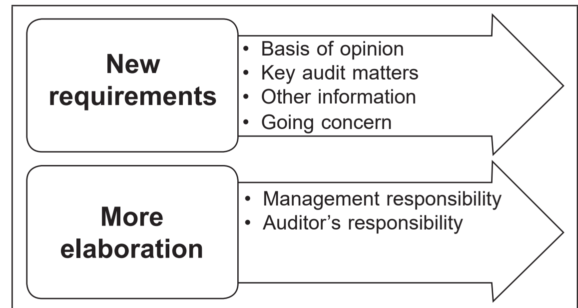
changed, one can take a view that format of IFC report is not required to be changed. Alternatively, as a better practice, there is no harm in changing the format of IFC report in line with SA 700 (revised).

- SA 700 (revised) is not applicable in case of engagements like reviews, compilation or agreed upon procedures. Therefore, format of review report (e.g., limited review report in case of quarterly results of listed companies where format is prescribed by SEBI) is not required to be changed as per SA 700 (revised).

B. Revised structure of the audit report is as under

- Title
- Addressee
- Auditor's opinion
- Basis for opinion
- Going concern, where applicable
- Key audit matters
- Other information, where applicable
- Management responsibilities for the financial statements
- Auditor's responsibilities for the audit of the financial Statements
- Other reporting responsibilities
- Signature of the auditor
- Place of signature
- Date of the auditor's report

Some of the elements mentioned above are new requirements and in few cases there is more elaboration. This is explained by the chart below:



C. Analysis of the elements of the audit report

1. ***Addressee***

The auditor's report is addressed to those for whom it is prepared. Examples are given below:

- In case of company – it should be addressed to members of company
- In case of partnership firm/limited liability partnership – it should be addressed to partners

2. ***Opinion paragraph & Basis of Opinion***

- Sequence of the paragraphs have changed. Now audit report begins with the Opinion paragraph followed by the Basis of Opinion paragraph so that user's attention is attracted to the most relevant part of the audit report.
- Basis of Opinion paragraph is also required to be given when there is an unmodified opinion and it includes the following:
  - o Audit is conducted in accordance with the SAs and whether the audit evidence obtained is sufficient and appropriate to provide a basis for the opinion.

- o Affirmative statement that the auditor is independent of the entity.
- o Auditor has fulfilled the other relevant ethical responsibilities relating to the audit which includes the Code of Ethics issued by the ICAI and ethical requirements under the provisions of the Companies Act, 2013 and the Rules thereunder.

3. *Going concern*

- A new paragraph on management responsibility for assessment of going concern and also auditor's responsibility has been added in the respective sections.
- In cases where there is a material uncertainty as regards going concern a separate paragraph has to be added. This requirement was already applicable through revised SA 570 from financial year 2017-18; however the same is now incorporated in SA 700 (revised) to ensure consistency.
- It is not necessary for all entities to have separate paragraph on going concern. It is only where in auditor's judgment, where there is a material uncertainty that casts a significant doubt on the ability of an entity to continue as a going concern and disclosure in the financial statements are adequate in accordance with SA 570 (revised).

4. *Key audit matters (KAM)*

- These are matters that were of most significance in auditor's judgment in the audit of the financial statements of the current period. Auditor has to describe the key audit matter and mention audit procedures followed in respect of these matters.
- New SA 701 deals with the guidance on how to report on KAM.
- It is compulsory in case of listed entities or in case of unlisted entities it is voluntary i.e., where the auditor believes that such matters are required to be reported.

5. *Other information in annual report*

- These are the information which are included in the annual report of the company e.g., Board of directors report and annexures thereto, management discussion and analysis, corporate governance, etc.
- SA 720 (revised) deals with the guidance on how to report on other information. This includes manner of reporting in different scenarios e.g., other information received prior or after the date of audit report, information received partly prior and partly after the date of audit report, if material mis-statements are identified and not corrected by the management etc.

6. *Management responsibilities for the financial statements*

It is important for the users to know that auditor is not responsible for preparation of financial statements. This paragraph explains that responsibility of preparation of financial statements is of board of directors in case of company and partners in case of partnership firm/LLP. In some entities, the appropriate reference may be to those charged with governance.

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If those responsible for preparing financial statements are different than those responsible for the oversight of the financial reporting process, than auditor's report shall also identify those responsible for the oversight of the financial reporting process e.g., in case of consolidated financial statements, holding company's management will be responsible for preparing consolidated financial statements and board of directors of respective companies included in the group and of associates or joint venture are responsible for overseeing the financial reporting process

7. ***Auditor's Responsibilities for the Audit of the Financial Statements***

With an objective to bring about more clarity as regards auditor's role and responsibility the standard has expanded the standard paragraph on auditor's responsibility. This includes more clarity about auditor's responsibility with respect to

- o Fraud
- o Internal financial control
- o Going concern
- o Communication with respect to key audit matters
- o Accounting policies and accounting estimates
- o Evaluating the overall presentation, description of materiality, structure and content of the financial statements and disclosures, group audits, and communications with those charged with governance.

It is important to note that expansion in this para does not mean that auditor's responsibilities have increased. It is only elaboration of responsibilities which are otherwise also existing.

Since length of auditor's responsibility section has increased, SA 700(revised) provides that certain parts of the description may be presented in an appendix to the auditor's report. Where law, regulation or applicable auditing standards expressly permit then the reference of website of an appropriate authority can also be given. Presently, under Companies Act, 2013, there is no reference of appropriate authority. Therefore, auditor should include it either in the body of the auditor's report or give it as an annexure.

In case of non-corporate entities or companies where reporting on internal financial control is not applicable suitable modification should be done to the formats provided in the illustrative audit reports.

There is now a requirement to be mention about the materiality considered while performing the audit. The implementation guide/the illustration has provided standard paragraph which can be included in the auditor's report. There is no requirement to provide amount of materiality which is considered for the purpose of execution of audit. In many jurisdictions across the world who have adopted ISA 700 (revised), there are instances where the amount of materiality has been included in the auditor's report.

8. ***Other reporting responsibility***

In this paragraph, the auditor is required to report on specific reporting requirements as required by the relevant law. For example reporting requirement under Companies Act, 2013.

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9. Signature & place of the Auditor

Auditor can sign the audit report at a place other than the city where the registered office of the entity is situated. Directors and auditor need not sign the financial statements at the same location. Auditor should mention the location where he signs the audit report.

10. Date of auditor's report

It cannot be prior to management has asserted that they have taken the responsibility for the financial statement. E.g., in case of company, it is the date when board of directors approves the financial statements. It is possible that it is dated after the date of the board meeting in which the financial statements are approved.

D. Reporting requirement in specific circumstances

Particulars	*Guidance*
When law or regulation prescribes format different than SA 700 (revised)	• To the extent allowed, auditor should change the prescribed format to bring in line with the SA e.g., add responsibility paragraph if it is not there.
	• In case of Form 3CB (tax audit report) there is no option to change the format and layout. The paragraphs relating to auditor responsibility and management responsibility should be added in the observations and comments section to ensure compliance with SA 700 (revised).
	• Different layout would be acceptable as long as basic elements prescribed in para 49 of SA 700 (revised) are given in the audit report e.g., title, management responsibility, auditor's responsibility, etc.
	• If it is not possible to change the format and it is not possible to incorporate the requirements of the SA 700 (revised) then in such cases, auditor may consider Emphasis of Matter or give Modified opinion.
When a statute or court order or government directive/ permission allows an entity to prepare financial statements without meeting a GAAP requirement	• An entity may be permitted to account for a certain type of income or expenditure on cash basis which is not permitted by the Accounting Standards.
	• This is not a non-compliance with the framework but compliance with a modified framework.
	• If the effect is material, the auditor should describe the resultant deviation from the framework in sufficient detail in an Emphasis of Matter paragraph.

Particulars	*Guidance*
When supplementary information presented with the financial statements or where law or regulation requires additional information that is outside the scope of the applicable financial reporting framework	• As far as possible, suggest auditee to give such information separately from financial statements e.g., Director's report.
	• In normal circumstances, auditor will have to audit this information and report on it, if it is part of financial statement.
	• If the management doesn't want it to be audited, mention that it is unaudited.
	• In the above instance, auditor will still have reporting responsibilities under SA 720 (revised).

Standard on Auditing (SA) 720 (Revised)- The auditor's responsibilities relating to other information

A. Overview and applicability

From the perspective of the reader of the annual report, it is expected that there is consistency in the information given in the financial statements and other information included in the annual report.

There could also be instances where information given in the director's report may affect the auditor's opinion on the audited financial statements e.g., management may have given additional information in the director's report as regards certain litigation which are going on whereas auditor may not be aware of or had limited information based on which he would have concluded his verification. In some cases, it is possible that management has disclosed certain financial/non-financial information which is not consistent with the audited financial statements.

The evidence or knowledge obtained during the audit will be very important to correlate and verify other information. It should be noted that the auditor's responsibilities under this SA do not constitute an assurance engagement on other information or impose an obligation on the auditor to obtain assurance about the other information.

SA 720 (revised) deals with auditor's responsibilities and guidance on reporting relating to other information (financial or non-financial) included in entity's annual report. As per the existing SA 720, auditor was required to verify other information included in the annual report like board of directors report etc., however there was no specific requirement to report.

This SA is effective for audits of financial statements for periods beginning on or after 1st April, 2018. The reporting requirements in SA 720 (revised) is not be applicable in case of non-corporate entities (partnership firm/LLP/individual/trust).

B. What is other information

Financial or non-financial information (other than financial statements and the auditor's report thereon) included in an entity's annual report.

In case of listed companies

- Board of directors report including its annexures
- Management discussion and analysis
- Corporate governance report

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In case of unlisted companies
Board of director's report including its annexures.

As stated above, it includes both financial and non-financial information. Some of the examples are given below:

Examples of other information — where amounts are involved

- Items in a summary of key financial results, such as net income, earnings per share, dividends, sales and other operating revenues, and purchases and operating expenses
- Liquidity and capital resource information, such as cash, cash equivalents and marketable securities; dividends; and debt, capital lease and minority interest obligations
- Financial measures or ratios, such as gross margin, return on average capital employed, return on average shareholders' equity, current ratio, interest coverage ratio and debt ratio. Some of these may be directly reconcilable to the financial statements
- Amounts involved in, and related financial effects of, off-balance sheet arrangements

Examples of other information — where amounts are not involved

- Descriptions of guarantees, contractual obligations, litigation or environmental liability cases, and other contingencies
- Descriptions of changes in legal or regulatory requirements, have a material impact on the entity's financials
- Descriptions of trends in market prices of key commodities or raw materials
- Explanations of specific factors influencing the entity's profitability in specific segments

C. What is not included

Examples of reports that, when issued as standalone documents, are not typically part of the combination of documents that comprise an annual report (subject to law, regulation or custom), and that, therefore, are not other information within the scope of this SA, include:

- Separate industry or regulatory reports (for example, capital adequacy reports), such as may be prepared in the banking, insurance, and pension industries
- Corporate social responsibility reports
- Sustainability reports
- Diversity and equal opportunity reports
- Product responsibility reports
- Labour practices and working conditions reports
- Human rights reports
- Other regulatory filings with the Government agencies such as the Registrar of Companies.

Further, other information also does not include:

- Preliminary announcements of financial information
- Securities offering documents, including prospectuses

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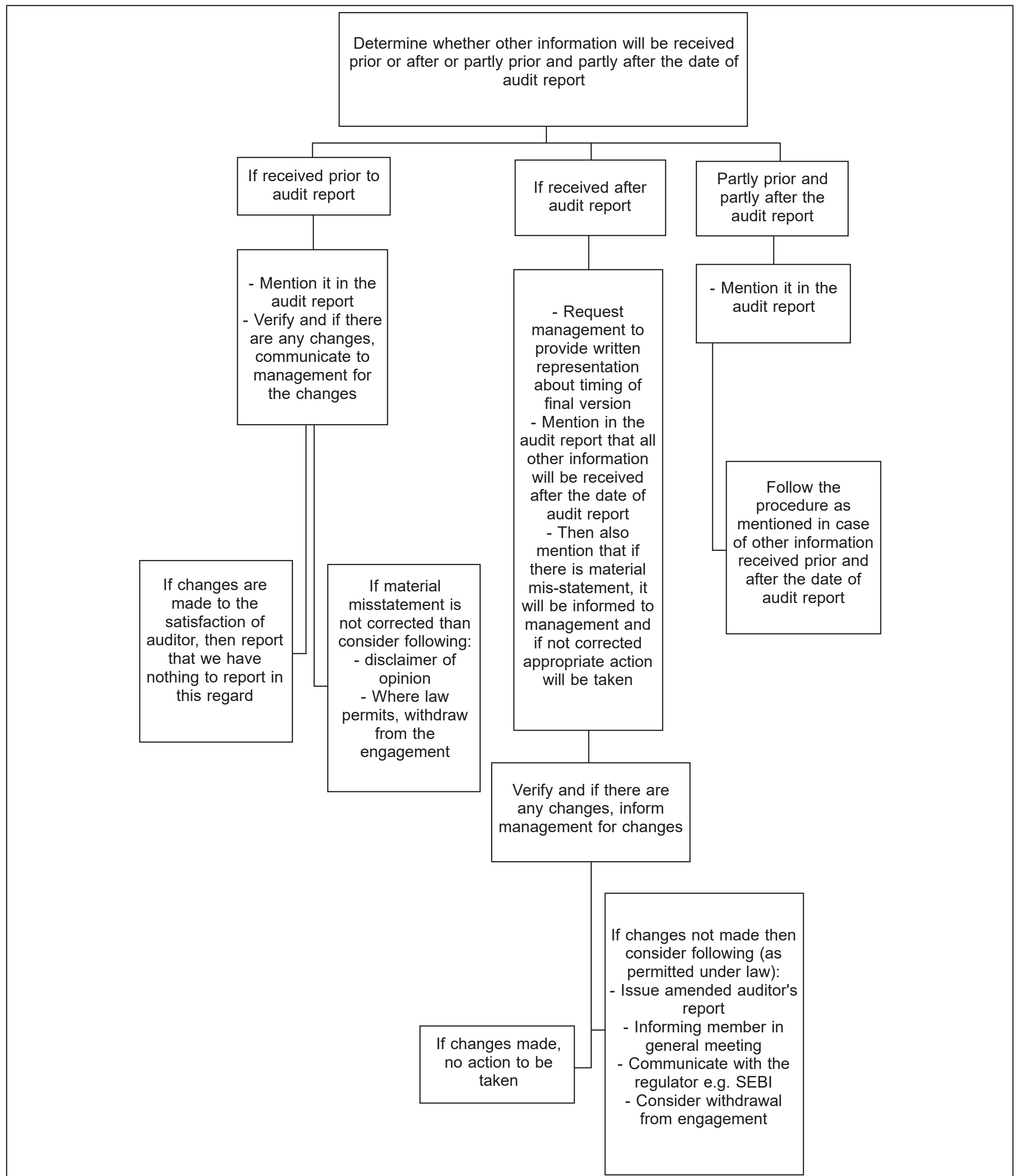
D. Key elements and audit steps



E. Reporting requirements

The following are the key elements of the reporting requirements in the audit report

- Statement that management is responsible for other information
- Identification of other information including what is obtained prior to the date of audit report and what is expected to be received subsequent to the date of audit report
- Statement that audit opinion does not cover the other information and hence no opinion is expressed on the same
- Description of auditors responsibility i.e., reading the other information and considering the same as required by this standard
- When information has been received prior to the date of the audit report, an affirmative statement that there is nothing to report on the other information or there is uncorrected material misstatement in the other information.

F. Common reporting issues and guidelines

Particulars	*Guidance*
When there is a qualification in the auditor's report	• Auditor should verify that how it is communicated in the other information. E.g., qualified opinion on the financial statements because of non-disclosure of directors' remuneration as required by the applicable financial reporting framework may have no implications for the reporting required under this SA.
In case of private companies, there is no annual report	• In case of private companies, there is no requirement under law to issue of annual reports. There is only board of director's report which is there as other information. Therefore, in case of private companies, auditor has to consider only board of director's report for the purpose of verification and reporting under this SA.
In case of unlisted non-corporate entities (e.g. partnership firm) what is auditor's responsibility under this standard	• Though there is no reporting requirement, all the other requirements in SA 720 (revised) will be equally applicable to audits of all unlisted entities i.e., auditor's responsibility as regards verification of other information.

G. Tips for auditors

- Changes required in engagement letter with respect to reporting responsibilities for other information
- At planning stage, auditor should what is the other information and design appropriate audit steps
- Discuss with management, whether other information will be received prior or after the date of audit report
- Time management – since this would be one of last information to be received, care needs to be taken for verification of the same
- Communicating the changes which are required in the other information
- Ensure that the changes are done appropriately by the management
- Auditor should know what options are available if there is material misstatements which are not corrected by the management
- Documentation
  - o Documentation of the procedures performed
  - o The final version of the other information should be kept in the audit file

Concluding remarks

In our view, changes in SA 700 (revised) and 720 (revised) along with changes in other SAs which are related to reporting by the auditor will bring more transparency and increase credibility of the audit report. ICAI's intention behind making these changes is to ensure that reader of the audit report focuses on the aspects relevant to them and at the same time safeguard auditor's responsibility.

Reader will have greater clarity and understanding of the management responsibility and auditor's responsibility, increase the reliability on the other information in view of comprehensive reporting by auditors not only on the financial statements but also on the other information. One fallout which we can highlight is on the length of the audit report. Therefore, it is to be seen in coming days whether objective to bring more clarity and transparency in the audit report is fetching its intended result.

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> Upon ages of struggle a character is built. Be not discouraged. One word of truth can never be lost; for ages it may be hidden under rubbish, but it will show itself sooner or later. Truth is indestructible, virtue is indestructible, purity is indestructible.
>
> — *Swami Vivekananda*

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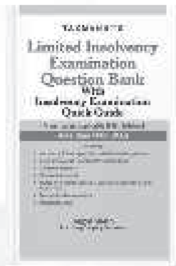

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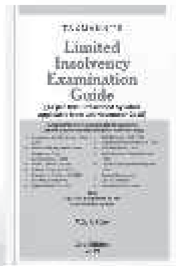

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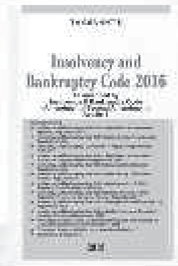

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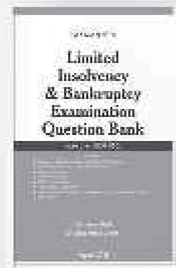

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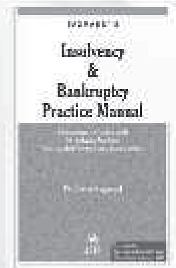

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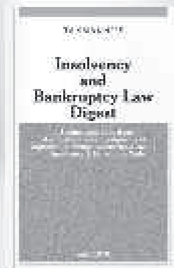

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SCAN & BUY

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Rahul Sarda, *Advocate*

Best of the Rest

Arbitration clause in unstamped agreement – whether arbitrator can be appointed by Courts?

The appeal arose out of a sub-contract given by the Appellant to the Respondent in respect of work to be done for installation of a geotextile tubes embankment with toe mound at village Pentha in Odisha for protection against coastal erosion. The agreement contained an arbitration clause.

Disputes arose between the parties and the Appellant terminated the sub-contract. As a result, the Respondent wrote to the Appellant stating that as disputes and differences had arisen between the parties, notice was given of appointment of a sole arbitrator. The Appellant objected to the appointment as per the Appellant, the appointment was premature. The Respondent, therefore, filed a petition under Section 11 of the Arbitration and Conciliation Act, 1996 before the Bombay High Court and the Bombay High Court allowed the Section 11 petition and appointed a sole arbitrator to adjudicate upon disputes and differences which have arisen between the Appellant and the Respondent.

The agreement between the parties was undisputedly unstamped, and hence, the question raised in this appeal before the Supreme Court was as to what was the effect of an arbitration clause contained in a contract which was required to be stamped.

The Supreme Court referred to its judgment in the case of *SMS Tea Estates (P) Ltd. vs. Chandmari Tea 2 Co. (P) Ltd., (2011) 14 SCC 66* and particularly the observations wherein the Court had observed that if a document was found to be not duly stamped, Section 35 of the Stamp Act barred the said document from being acted upon and consequently, even the arbitration clause therein could not be acted upon.

The Supreme Court held that the Indian Stamp Act was applicable to the agreement or conveyance as a whole and therefore, it was not possible to bifurcate the arbitration clause contained in such agreement or conveyance so as to give it an independent existence, as had been contended for by the Respondent. When an arbitration clause was contained "in a contract", the agreement only became a contract if it was enforceable by law. However, under the Indian Stamp Act, an agreement did not become a contract, namely, that it was not enforceable in law, unless it was duly stamped. The Supreme Court also rejected the argument of the Respondent that the obligation to pay stamp duty was on the Appellant and the Appellant could not take advantage of its own wrong on the reasoning that such argument was not available when it came to application of mandatory provisions of law.

Garware Wall Ropes Ltd. vs. Coastal Marine Constructions & Engineering Ltd. - 2019 SCC OnLine 515 (SC).

One-sided clauses in builder's agreement – Amounts to unfair trade practice – Not enforceable against the

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flat purchaser if it can be shown that the flat purchaser had no choice but to sign the agreement.

Statutory appeals were filed under Section 23 of the Consumer Protection Act, 1986 to challenge the final judgment and order passed by the National Consumer Disputes Redressal Commission. The Appellant–builder launched a residential project in the city of Gurugram. The Respondent–flat purchaser entered into an Apartment Buyer's Agreement dated 8-5-2012 with the Appellant to purchase an apartment in the said project.

As per Clause 11.2 of the Agreement, the Appellant was to make all efforts to apply for the Occupancy Certificate within 39 months from the date of excavation, with a grace period of 180 days. The excavation of the project commenced on 4-6-2012, and hence, as per Clause 11.2 of the Agreement, the Appellant was required to apply for the Occupancy Certificate by 4-9-2015, or within a further grace period of 6 months i.e. by 4-3-2016, and offer possession of the flat to the Respondent. The Appellant however failed to apply for the Occupancy Certificate as per the stipulations in the Agreement. The Respondent filed a case with the National Consumer Disputes Redressal Commission alleging deficiency of service on the part of the Appellant for failure to obtain the Occupancy Certificate, and hand over possession of the flat and prayed for (i) refund of entire consideration with interest @ 18% p.a.; (ii) Compensation of ₹ 10,00,000/- for mental agony, harassment etc.; (iii) refund of wrongfully charged taxes i.e. Service Tax and other charges along with interest @ 18% p.a.; and, (iv) litigation costs of ₹ 1,00,000/-.

The National Commission passed an *ex-parte* Interim Order restraining the Appellant from cancelling the allotment made in favour of the Respondent during the pendency of the Consumer Case. During the pendency of the proceedings before the National Commission, the Appellant obtained Occupancy Certificate on 23-07-2018, and issued a possession letter to the Respondent on 28-08-2018. The Appellant submitted before the National Commission that since the construction of the apartment was complete, and the Occupancy Certificate had since been obtained, the Respondent must be directed to take possession of the apartment, instead of directing refund of the amount deposited. However, the Respondent submitted that he was not interested in taking the possession of the flat after an inordinate delay of almost 3 years. The National Commission allowed the Consumer Complaint filed by the Respondent, and held that since the last date stipulated for construction had expired about 3 years before the Occupancy Certificate was obtained, the Respondent could not be compelled to take possession at such a belated stage and directed the Appellant to refund the entire consideration with interest @ 10.70% p.a. relying on Rule 15 of the Haryana Real Estate (Regulation and Development) Rules, 2017, except for the period for which the Interim Order dated 6-2-2017 was in operation.

Before the Supreme Court, the Appellant contended that the Respondent was not entitled to refund of the amount deposited, since the Apartment Buyer's Agreement was not terminated by the Respondent in accordance with Clause 11.5 (ii) of the Agreement, which stipulated that the allottee had to terminate the Agreement by giving a Termination Notice of 90 days to the Developer.

On behalf of the Respondent, it was *inter alia* argued that clauses of the Agreement were one-sided inasmuch as the builder could charge interest @ 18% p.a. for delayed payments by a flat purchaser while a flat purchaser would be entitled to interest only @ 9% p.a. in case of delay by the builder in handing over the possession of the flat.

The Supreme Court held that considering the delay in handing over possession of the flat to the Respondent, the Respondent was justified in terminating the Agreement. It was also held that the Agreement revealed stark incongruities between the remedies available to both the parties – for instance, (i) the Agreement entitled the Appellant to cancel the allotment and terminate the Agreement, if any installment remained in arrears for more than 30 days while if the Appellant failed to deliver

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possession of the apartment within the stipulated period, the Respondent had to wait for a period of 12 months after the end of the grace period, before serving a termination notice of 90 days on the Appellant; (ii) the Agreement entitled the Appellant to serve a termination notice upon the Respondent for breach of any contractual obligation while if the Respondent failed to rectify the default within 30 days of the termination notice, then the Agreement automatically stood cancelled, and the Appellant had the right to forfeit the entire amount of earnest money towards liquidated damages and if the Respondent failed to exercise his right of termination within the time limit provided, then he shall not be entitled to terminate the Agreement thereafter, and shall be bound by the provisions of the Agreement.

The Supreme Court held that the contractual terms of the Agreement dated 8-5-2012 were *ex-facie* one-sided, unfair, and unreasonable and the incorporation of such one-sided clauses in an agreement constituted an unfair trade practice as per Section 2 (r) of the Consumer Protection Act, 1986 since it adopted unfair methods or practices for the purpose of selling the flats by the builder. The Court further held that a term of a contract would not be final and binding if it is shown that the flat purchasers had no option but to sign on the dotted line, on a contract framed by the builder and the Agreement could not bind the Respondent. The National Commission had rightly relied on Rule 15 of the Haryana Real Estate (Regulation and Development) Rules, 2017 to award interest @ 10.7% despite lower interest rate being prescribed in the Agreement.

Pioneer Urban Land & Infrastructure Ltd. vs. Govindan Raghavan - 2019 SCC OnLine 458 (SC).

Section 138 complaint under Negotiable Instruments Act – Dishonour of cheque – Payment of sale consideration under an agreement to sell – Constitutes a payment for due discharge of debt – Complaint maintainable

The appeal arose from an order of the learned Single Judge who allowed a petition under Section 482 of the Code of Criminal Procedure, 1973 and quashed the complaints instituted by the Appellants under Section 138 of the Negotiable Instruments Act, 1881. Claiming to be owners of certain agricultural land, the Appellants entered into an agreement to sell dated 28th May 2013 with the Respondent for a consideration of ₹ 1.75 crore. The agreement records that an amount of ₹ 1.25 crore was paid in cash and as for the balance, two post-dated cheques were issued, each in the amount of ₹ 25 lakh issued by the Respondent in favour of the Appellants. Together with the agreement, the Appellants executed a General Power of Attorney in favour of the respondent.

The cheques of ₹ 25 lakh each were returned unpaid with the remarks "Insufficient funds". After issuing legal notices, the Appellants instituted complaints under Section 138 of the Negotiable Instruments Act, 1881. Process was issued by the Judicial Magistrate, First Class and the applications seeking discharge preferred by the Respondent were dismissed.

The Respondent then filed a petition under Section 482 CrPC before the High Court. While allowing the complaint, the High Court has adverted to Clause 4 of the agreement between the parties which is in the following terms:

> *"That on the above property of the seller there is no family dispute of any type nor is any case pending in the court. If due to any reason any dispute arises then all its responsibility would remain of the selling party and the payment of cheques would be after the resolution of the said disputes."*

The High Court held that a suit in respect of the land was pending before the Additional Sessions Judge since 2nd September, 2011 in which the complainants were arraigned as parties and as per Clause 4, the cheques could not be presented for payment. Holding that the Respondent did not owe any money to the Complainants, the complaint under Section 138 was quashed by the High Court.

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The Supreme Court held that the cheques were issued under and in pursuance of the agreement to sell. Though it is well-settled that an agreement to sell does not create any interest in immovable property, it nonetheless constitutes a legally enforceable contract between the parties to it. A payment which is made in pursuance of such an agreement is hence a payment made in pursuance of a duly enforceable debt or liability for the purposes of Section 138. The Supreme Court also observed that the Respondent had, acting under the General Power of Attorney, entered into a subsequent transaction.

The Court further held that the question as to whether there was a dispute as contemplated in clause 4 of the Agreement to Sell which obviated the obligation of the purchaser to honour the cheque which was furnished in pursuance of the agreement to sell to the vendor, could not be the subject matter of a proceeding under Section 482 and was a matter to be determined on the basis of the evidence which may be adduced at the trial.

The Court also rejected finding of the learned Single Judge of the High Court that the cheques were not issued for creating any liability or debt, but 'only' for the payment of balance consideration and that in consequence, there was no legally enforceable debt or other liability. Therefore, recourse to the jurisdiction of the High Court under Section 482 was held to be a clear abuse of process and the order passed by the High Court in the petition under Section 482 CrPC was held unsustainable.

Ripudaman Singh vs. Balkrishna (2019) 4 SCC 767.

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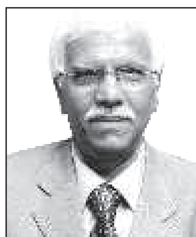

Kishor Vanjara, *Tax Consultant*

Tax Articles for Your Reference

Articles published in Taxman, The Bombay Chartered Accountant Journal (BCAJ), The Chamber's Journal (C J), The Chartered Accountant Journal (CAJ), All India Federation of Tax Practitioners Journal (AIFTPJ), All India Federation of Tax Practitioners Indirect Tax & Corporate Laws Journal (AIFTP Indirect Tax), Goods & Sales Tax Practitioners Association of Maharashtra (GSTPAM), Sales Tax Review (STR), Income Tax Report (ITR), Times of India and Economic Times for the period April 2019 To May 2019 has been arranged and indexed topic-wise.

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NOTICE OF ELECTION

To
The Members,
The Chamber of Tax Consultants,
Mumbai

The election of the President and fourteen Members of the Managing Council for the ensuing year 2019-20 shall take place on **Monday, May 6th, 2019 at the Office of The Chamber of Tax Consultants, 3, Rewa Chambers, Ground Floor, 31, New Marine Lines, Mumbai–400 020.**

Nominations in the prescribed form should be filed so as to reach the office of the CTC not later than **6.00 p.m**. on **Tuesday, April, 23rd 2019**. The nomination forms shall be available at the CTC office from **Wednesday, April, 17th 2019.**

FOR AND ON BEHALF OF THE MANAGING COUNCIL OF
The Chamber of Tax Consultants

Sd/- Sd/-
ANISH M. THACKER/PARAG S. VED
Hon. Jt. Secretaries

Place: Mumbai

Dated: 13th February, 2019

Office :
3, Rewa Chambers, 31, New Marine Lines, Mumbai-400 020.

Notes:

1. Ordinary and Life Members are **only** eligible to vote at the election.
2. A Member who has completed at least **two full years** as a member shall be entitled to contest for the post of Managing Council member or to propose or second a candidate for the election. Each such member can propose not more than **three** candidates. The candidate for the post of President should have completed ten years of post qualification experience relating to tax laws or any branch of accountancy or company secretarial practice.
3. Members whose membership subscription is in arrears shall not be entitled to contest any election or to propose or second any candidate for the election or to vote at the election.
4. Withdrawal of nomination for the elections can be made by the candidate on or before 6.00 p.m. on **Monday, April 29th, 2019**.
5. If elections are required to be held, the names of the valid candidates shall be intimated through the website of the Chamber as well as through a circular. The Members are requested to check through these mediums.
6. If elections are not required to be held, due to any reason whatsoever, the same shall be intimated through the website of the Chamber as well as through the Notice Board at the Chamber's office. The Members are requested to check through these mediums.
7. The voting, if required, will commence at 11.00 a.m. and shall end at 5.00 p.m.
8. The above is only a gist of the Elections Rules. Please read Election Rules of the Chamber carefully on the website www.ctconline.org.
9. Please note that the Election Committee comprising of the following persons, is constituted for this purpose.

   (1) Mr. Keshav Bhujle, (2) Mr. Ajit Rohira, (3) Mr. Bhavesh Vora.

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CA Anish Thacker & CA Parag Ved, *Hon. Jt. Secretaries*

The Chamber News

Important events and happenings that took place from 7th May, 2019 to 7th June, 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 17th May, 2019 are as under:—

Type of Membership	No. of Members
Life Member	15
Ordinary Member	30
Student Member	2
Associate Member	4

II. PAST PROGRAMMES

1. IT CONNECT COMMITTEE

A Technology Clinic was held on 29th May, 2019 at CTC Conference Room. The clinic was addressed by panellists, CA Dinesh Tejwani, CA Uday Shah, CA Mitesh Katira, CA Pranay Kochar and was moderated CA Amit Salla.

2. INTERNATIONAL TAXATION COMMITTEE

The "5th International Study Tour" was held from 25th May, 2019 to 5th June, 2019 at Central Europe. The tour's highlight was a visit to Vienna University of Economics and Business. The Vice-Rector Dr. Michael Lang deliberated current International Tax issues with the participants which was very much appreciated by those present.

3. MEMBERSHIP & PR COMMITTEE (JOINTLY WITH TAX PRACTITIONERS ASSOCIATION KALYAN AND B. K. BIRLA COLLEGE)

A Half Day Seminar on Annual Returns and GST Audit was held on 18th May, 2019 at New Seminar Hall, B. K. Birla College, Kalyan West. The seminar was addressed by CA Jignesh Kansara & CA Keval Shah.

4. **PUNE STUDY GROUP**

A meeting on Contemporary issues in Benami Transaction Law and Prevention of Money Laundering Act was held on 11th May, 2019 at ELTS, Plot No. 419, Model Colony, Gokhale Cross Road, Pune. The seminar was addressed by Shri Ashwani Taneja, Advocate and Former ITAT Member.

III. FUTURE PROGRAMMES

1. **ACCOUNTING & AUDITING COMMITTEE & CORPORATE CONNCECT COMMITTEE**

A "Study Course on Valuation" is scheduled to be held on 8th June, 2019 at IMC, Churchgate.

2. **COMMERCIAL & ALLIED LAWS AND CORPORATE CONNECT COMMITTEE**

A Seminar on issues related to the Insolvency & Bankruptcy Code and Resolution of Distressed Assets is scheduled to be held on 15th June, 2019 at IMC, Churchgate.

3. **COMMERCIAL & ALLIED LAWS AND DIRECT TAXES COMMITTEE**

A Workshop on the Bemani Transactions Amendment Act, 2016 and Prevention of Money Laundering Act, 2002 is scheduled to be held on 29th June, 2019 at Hotel West End, Churchgate, Mumbai.

4. **DIRECT TAXES COMMITTEE**

A Half Day Workshop on Return Filing provisions under the Income-tax Act is scheduled to be held on 28th June, 2019 at IMC, Churchgate.

5. **INTERNATIONAL TAXATION COMMITTEE**

The "13th Residential Refresher Course on International Taxation", 2019 is scheduled to be held from 20th June, 2019 to 23rd June, 2019 at The Grand Bhagwati, Surat.

6. **MEMBERSHIP & PUBLIC RELATIONS COMMITTEE**

A Full Day Seminar on Direct Taxes at Nagpur is scheduled to be held on 29th June, 2019 at Hotel Centre Point, 24, Central Bazar Road, Ramdaspeth, Nagpur-440010

7. **PUNE STUDY GROUP**

A Full Day Seminar on Contentious Issues in Real Estate Related Transactions is scheduled to be held on 15th June, 2019 at ELITS, Plot No. 419, Model Colony, Gokhale Cross Road, Pune.

8. **STUDENT COMMITTEE**

A Student Orientation Course is scheduled to be held from 13th June to 15th June, 2019 at Juhu Jagruti Hall, Mithibhai College, Vile Parle, Mumbai.

9. **STUDENTS COMMITTEE AND MEMBERSHIP & PUBLIC RELATIONS COMMITTEE**

The 5th CTC Football Cup is scheduled to be held on 10th August, 2019 at Dr. Antonia Da Silva High School, Dadar West.

(For details of the future programmes, kindly visit www.ctconline.org or refer The CTC News of June, 2019)

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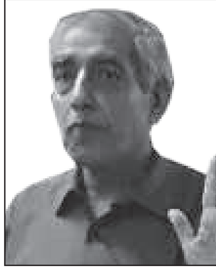
Bengaluru Study Group

Bengaluru Study Group Meeting was held on 17th May, 2019 at FKCCI, 3rd Floor, Hall No. 4, K. G. Road, Bengaluru

CA S. Ramasubramanian addressing the delegates on the topic "Analysis of Penalty Provisions u/s. 270A"



CA Naginchand Khincha addressing the delegates on the topic "Analysis of Penalty Provisions related to Search, Section 115BBE, Section 269ST & Penalty u/s. 271DA"

IT Connect Committee

Technology Clinic was held on 29th May, 2019 at CTC Conference room

Panelist answering the queries. Seen from L to R: CA Pranay Kochar, CA Dinesh Tejwani, CA Uday Shah, CA Amit Salla (Moderator) and CA Mitesh Katira

International Taxation Committee

FEMA Study Circle on "Discussion on upcoming RRC Panel Questions" was held on 3rd & 14th May, 2019 at CTC Conference Room

CA Vishal Shah (Group leader) addressing the delegates

CA Natwar Thakrar (Chairman) addressing the delegates

CA Hardik Mehta (Group leader) addressing the delegates

CA Manoj Shah (Chairman) addressing the delegates

Direct Taxes Committee

Webinar on "TDS u/s. Section 195, 15CA/CB & Lower Deduction" was held on 18th May, 2019

CA Sanjay Chokshi

Indirect Taxes Committee

Indirect Taxes Study Circle Meeting on "Issues in Form GSTR-9 and GSTR-9C" was held on 23rd May, 2019 at Jai Hind College, A. V. Room, 4th Floor, A Road, Churchgate

CA Payal Shah addressing the delegates

CA Jinit Shah addressing the delegates

Membership & PR Committee

Half Day Seminar on Annual Return and GST Audit jointly with Tax Practitioners Association Kalyan and B. K. Birla College was held on 18th May, 2019 at New Seminar Hall, B. K. Birla College, Kalyan West

CA Jignesh Kansara addressing the delegates

CA Keval Shah addressing the delegates

Pune Study Group

Contemporary Issues in Benami Transactions Law and Prevention of Money Laundering Act was held on 11th May, 2019 at ELTIS, Model Colony, Pune

Mr. Ashwani Taneja, Advocate addressing the delegates

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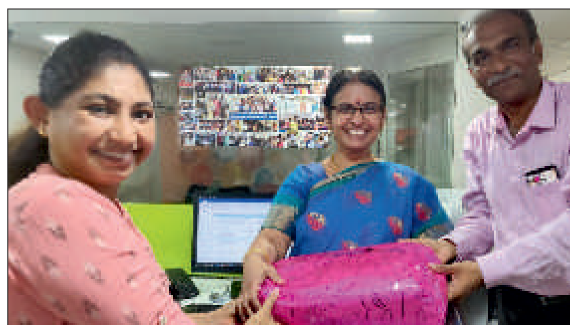
CTC was invited to give Pre-Budget Memorandum

CTC was invited to give Pre-Budget Memorandum by Ministry of Finance, New Delhi on 7th June, 2019. CBDT Chairmen Mr. P. C. Mody, Member CBDT Mr. Akhilesh Ranjan, Secretary TPL Mr. Kamlesh Varshney and other senior officers in Budget section were present at the meeting

CTC Team met Mr. P. K. Dash, Member CBDT in North Block, New Delhi on 7th June, 2019 to discuss various issues related to CPC processing, TRACES and other tax litigation matters.



A farewell to Ms. Rema Nair, Finesse Graphics & Prints Pvt. Ltd. We at CTC thank you for all the support and goodwill you have shown to us over the years. The sweet memories of working with you will be hard to forget

Membership & PR Committee

Full Day Seminar on Direct Taxes jointly with Tax Bar Association Amravati was held on 4th May, 2019 at Daimond Hall, Amravati

Release of the Program Souvenir at the Seminar by Chief Guest Shri Kishor Diwani, Advoacte. Seen from L to R: CA Jagdish Punjabi (Speaker), CA Ratan Sharma (Secretary, TBA), CA R.R. Khandelwal (President, TBA), CA Anish Thacker (Hon. Joint Secretary, CTC), CA Nilesh Lathiya (Seminar Convenor), Mr. Dharan Gandhi, Advocate (Speaker), CA Abhitan Mehta (Speaker) and CA Lalit Tambe

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International Taxation Committee

5th International Study Tour was held from 25th May, 2019 to 5th June, 2019 at Central Europe with 91 Delegates

Delegates with Prof. Dr. Michael Lang, Vice Rector - Vienna University

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