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ACCOUNTING UPDATES

INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA (ICAI)

EAC OPINION

Classification of the Project as Inventory or Investment Property under Ind AS framework

Facts of the Case

A company (hereinafter referred to as 'the Company') is a public sector undertaking (PSU) under the aegis of Ministry of Housing and Urban Affairs, Government of India, established in the year 1960 as a construction arm of Government of India. The Company has achieved ***Navratna*** status in the year 2014. The Company as a group has four operational subsidiaries and several joint ventures under its umbrella. The Company operates into three business segments:

(a) Project Management Consultancy (PMC): In this segment, the Company executes cost plus contracts obtained on either nomination basis or through competitive bidding. The projects are executed by contractors appointed by the Company through transparent tendering process.

(b) Real EstateL In this segment, the Company works as a developer, procures land, gets the works executed by entering into contractual engagements with contractors and the project is sold in pre-construction and post-construction stages. Marketing is done by the Company itself.

(c) Engineering, Project and Construction (EPC) – In this segment, the Company takes contract at fixed prices and the work is executed through sub-contractors.

Indian Accounting Standards (Ind AS) were introduced on the Company w.e.f. 1 April 2016. The accounts of the financial year (FY) 2016-17 were prepared in accordance with Ind AS with comparatives of FY 2015-16 and opening balance sheet of 1 April 2015.

The Company is in the business of development of real estate property for sale in the ordinary course of business. 'A' Municipal Corporation (AMC) and the Company has developed a joint real estate property at J place with the Company's share at 76.98% and AMC's share at 23.02% (hereinafter referred to as 'the Project'). The Company executed the real estate project at J place in the year 2010 under joint operations with AMC.

The agreement between the Company and AMC was executed for sale of property after development. There was no intention of either the Company or AMC to lease out the property after development as per the Office Memorandum of Understanding (MoU) between the parties.

Upon completion of the Project, the Company has made multiple attempts to sell the property over the years. The Company appointed a property consultant M/S J *vide* Letter of Intent (LoI) dated 18 August 2008 for the purpose.

1st attempt: The Company called Expression of Interest (EOI) through advertisement in August 2009. Additionally, letters were also sent to 37 hotel agencies, but no response was received.

2nd attempt: In December 2009, letters were sent to 15 hotel agencies and an open advertisement was published in the leading newspaper for sale of property but nothing could be materialised.

3rd attempt: The Company again tried to sell the property in January 2011 by an open offer on website and advertisement in various newspapers, but no offer was received.

4th attempt: Finally, the Company tried to sell the space to Joint Operator, M/s AMC in January 2014, but that did not materialise either.

It is further submitted that a proposal for opening of the sale was also initiated and the same was submitted to the Board of Directors (BoD) and advertisement was published for sale, but could not be sold out due to non-availability of Completion/ Occupancy Certificate from the concerned Authority as well as incomplete Real Estate Regulatory Authority (RERA) formalities.

Since the property has already been completed and is habitable, a substantial portion of the Project has been utilised to generate income till the sale of the properties after receipt of the Occupancy Certificate and completion of RERA formalities. The space has been let out to some government authorities. The intention of the management towards the developed properties is to sell them in the market and not for let out and accordingly, rent agreement with the tenant is always entered for a short period of one or two years and with a vacation clause.

The Company has always tried to sell the property to recover its cost. Till date, the Company and AMC hold this property jointly. The temporary rental income earned from the property is shared in the profit-sharing ratio. The Company has recently received the Occupancy Certificate of the Project on 9 January 2024. Sale of the Project will be launched at the earliest after completing RERA and other statutory requirements.

Query

In view of the above, the opinion is sought from the Expert Advisory Committee of the ICAI as to whether the Company may continue to present share of assets in the project as 'Real Estate Inventory' or should transfer the same as 'Investment Property' or any other suitable treatment is required as per applicable Ind AS.

Points Considered by the Committee

The Committee notes that the basic issue raised in the query relates to classification of the Company's share of assets in the Project as 'Inventory' or 'Investment Property'. The Committee has, therefore, considered only this issue and has not considered any other issues that may arise from the Facts of the Case. Further, the Committee has answered the issue only from accounting perspective and not from legal perspective. The Committee has based its analysis on the information provided by the Company. Moreover, the Standards referred to hereinafter are Ind AS notified under the Companies (Indian Accounting Standards) Rules, 2015, and applicable as on 31 March 2024.

At the outset, the Committee notes that the Company has stated in the Facts of the Case that the arrangement is in the nature of joint operations; therefore, the Committee has proceeded on this premise and has not examined whether the joint arrangement in the extant case is in the nature of 'joint operation' or 'joint venture'.

In this context, the Committee notes the following extracts from Ind AS 40, 'Investment Property' and Ind AS 2, 'Inventories':

Ind AS 40

"Investment property is property (land or a building—or part of a building—or both) held (by the owner or by the lessee as a right-of-use asset) to earn rentals or for capital appreciation or both, rather than for:

(a) use in the production or supply of goods or services or for administrative purposes; or

(b) sale in the ordinary course of business."

"The following are examples of investment property:

(a) land held for long-term capital appreciation rather than for short term sale in the ordinary course of business.

(b) land held for a currently undetermined future use. (If an entity has not determined that it will use the land as owner-occupied property or for short-term sale in the ordinary course of business, the land is regarded as held for capital appreciation.)

(c) a building owned by the entity (or a right-of-use asset relating to a building held by the entity) and leased out under one or more operating leases.

(d) a building that is vacant but is held to be leased out under one or more operating leases.

(e) property that is being constructed or developed for future use as investment property.

The following are examples of items that are not investment property and are therefore outside the scope of this Standard:

(a) property intended for sale in the ordinary course of business or in the process of construction or development for such sale (see Ind AS 2 Inventories), for example, property acquired exclusively with a view to subsequent disposal in the near future or for development and resale.

(b) omitted

(c) owner-occupied property (see Ind AS 16 and Ind AS 116), including (among other things) property held for future use as owner-occupied property, property held for future development and subsequent use as owner-occupied property, property occupied by employees (whether or not the employees pay rent at market rates), and owner-occupied property awaiting disposal.

(d) [Refer Appendix 1]

(e) property that is leased to another entity under a finance lease."

"Judgement is needed to determine whether a property qualifies as investment property. An entity develops criteria so that it can exercise that judgement consistently in accordance with the definition of investment property and with the related guidance in paragraphs 7–13. Paragraph 75(c) requires an entity to disclose these criteria when classification is difficult."

"An entity shall disclose:

(a) its accounting policy for measurement of investment property.

(b) when classification is difficult (see above paragraph), the criteria it uses to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of business."

Ind AS 2

"Inventories are assets:

(a) held for sale in the ordinary course of business;

(b) in the process of production for such sale; or

(c) in the form of materials or supplies to be consumed in the production process or in the rendering of services."

The Committee notes from the above that classification of an asset as 'investment' or 'inventories' depends on its intended primary use for an entity. If an asset is essentially held for sale in the ordinary course of business, the same cannot be classified as investment property.

In this context, the Committee notes that the Company is in the business of development of real estate property for sale in the ordinary course of business. An agreement (MoU) between the Company and AMC was executed in the year 2005 for sale of property after development, salient features of which are reproduced below:

" AMC intends to develop its land/ PROPERTIES at J place, having commercial potential as real estate ventures. Whereas the Company, a Government of India enterprise, under the Ministry of Urban Development and Poverty Alleviation, has all the resources, capabilities and expertise for taking up development of commercial/ residential complexes and or buildings as real estate ventures as per the mutual requirements and in order to generate maximum revenue.

Both AMC and the Company, by pooling their resources and expertise, shall take up these projects to their mutual advantage."

For sale of the property, a professional marketing agency will be appointed. The marketing expenses/ brokerage would be borne by the Company and AMC for their respective areas.

In order to work out the profit element, the equity of both the partners shall be deducted from the total sale proceeds. The profits generated from the project, or alternately the built up space, after working out the weighted percentage based on the report of the 'Agency' would be shared between the Company and AMC in the ratio of their equity.

Upkeep and maintenance of the property after completion of construction in respect to sale/ leasing of the accommodation shall be done jointly by the respective owners of AMC and the Company with mutual understanding."

The Committee notes from the above terms of MoU and the other facts supplied by the Company that the Company along with AMC appointed a professional marketing agency for sale of the property. The Committee also notes from the facts of the case that the Company has made various attempts to sell the property, viz. appointing property consultants, advertising in leading newspapers, and attempting to sell it to the joint operator. However, the property could not be sold due to nonavailability of Completion/ Occupancy Certificate and pending RERA formalities. Therefore, as stated by the Company, in order to generate temporary rental income, the property has been let out to government authorities for short period. Further, it is also mentioned by the Company that it has recently received the Occupancy Certificate of the Project, and sale of the Project will be launched at the earliest after completing RERA and other statutory requirements. Thus, the intention of the management of the Company towards the developed properties, as demonstrated from the actions taken, has always been to sell them in the market and not for letting out. Therefore, the Committee is of the view that in the extant case, the Company's share in the property or project in the extant case is in the nature of 'Inventory' and not 'Investment Property'.

Opinion

On the basis of the above, the Committee is of the opinion that in the extant case, the Company's share in the property or project is in the nature of 'Inventory' and not 'Investment Property', as discussed above.

REGULATORY UPDATES

Institute of Chartered Accountants of India (ICAI)

Announcement Regarding Revised Criteria for Classification of Non-company entities for Applicability of Accounting Standards

ICAI has issued an Announcement dated 8 November 2024 prescribing revised criteria for classification of Non-company entities for applicability of Accounting Standards.

Categorisation of Non-company entities

Non-company entities are classified into two categories for the applicability of Accounting Standards:

1. Micro, Small and Medium Sized Entities (MSMEs) and
2. Large entities.

It has replaced the March 2021 announcement and introduces a revised approach to determine the extent of compliance required by each category of entities. This Announcement is not relevant for Non-company entities which may be required to follow Indian Accounting Standards (Ind AS) or Accounting Standards (AS) as per relevant regulatory requirements applicable to such entities.

Applicability to MSMEs and large entities

1. Micro, Small and Medium Sized Entity (MSME) means, a non-company entity:
   i. whose equity or debt securities **are not listed or are not in the process of listing** on any stock exchange, whether in India or outside India;
   ii. which is **not a bank, financial institution or an insurance company**;
   iii. whose **turnover (excluding other income) does not exceed INR 250 crore** in the immediately preceding accounting year;
   iv. which **does not have borrowings in excess of INR 50 crore** at any time during the immediately preceding accounting year; and
   v. which is **not a holding or subsidiary of an entity which is not a MSME.**

A non-company entity shall qualify as a MSME, if the conditions mentioned therein are satisfied as at the end of the relevant accounting period.

2. MSMEs are given certain exemptions/ relaxations, detailed in Annexure 1 of this announcement.
3. An MSME availing exemptions/ relaxations shall disclose their MSME status and compliance in financial statements by way of a note to its financial statements.
4. If an MSME no longer qualifies for an exemption/ relaxation, then the relevant standards become applicable from the current period and the previous period's figures do not need to be revised. These facts have to be appropriately disclosed in the financial statements.
5. Entities transitioning from non-MSME to MSME status shall not be qualified for exemption/ relaxation until the entity remains an MSME for two consecutive years.
6. An MSME may opt to avail partial exemptions/ relaxations from certain Accounting Standards provided, such exemptions/ relaxations must be disclosed clearly to avoid misleading users of the financial statements.

Applicability to Large Entities

Large entity is a **non-company entity that is not an MSME** and must comply with all the Accounting Standards.

The revised scheme for applicability of Accounting Standards to Non-company entities shall come into effect in respect of accounting periods commencing on or after 1 April 2024.

Reserve Bank of India (RBI)

Amendment to the Master Direction - Know Your Customer (KYC) Direction, 2016

RBI *vide* notification dated 6 November 2024 issued an Amendment to the Master Direction - Know Your Customer (KYC) Direction, 2016, aligning the KYC procedures with recent amendments to the Prevention of Money Laundering (Maintenance of Records) Rules, 2005 and the Unlawful Activities (Prevention) Act 1967.

Following are the key amendments:

1. **Customer Acceptance Policy -** Regulated Entities (REs) shall apply the Customer Due Diligence (CDD) procedures at the Unified Customer Identification Code (UCIC) level, eliminating the need for fresh CDD for KYC compliant customers opening another account or availing any other products or services from the same RE.
2. **On-going due diligence** - The 'Explanation' that "High risk accounts have to be subjected to more intensified monitoring" is applicable to paragraph 37 which addresses the extent of monitoring based on risk category of customer.
3. **CDD procedure and sharing KYC information with Central KYC Records Registry (CKYCR)** - REs shall upload/ update the KYC data for both individual and legal entity (LEs) customers opened prior to specified dates at the time of periodic updation or upon receiving updated customer KYC information. Further, additional or updated information shall be furnished within seven days or within such period as may be notified by the Central Government. CKYCR shall electronically inform all the reporting entities about the KYC updates and RE shall retrieve and update their KYC records accordingly.
4. **Annex II of the MD on KYC** - Based on the corrigendum dated 22 April 2024 issued by the Government of India to the Order dated 2 February 2021 regarding the 'Procedure for implementation of Section 51A of the Unlawful Activities (Prevention) Act, 1967', the designation of Central Nodal Officer for the UAPA has been changed from "Additional Secretary" to "Joint Secretary".

These amended provisions shall come into force with immediate effect.

This notification impacts all the Regulated Entities.

Reporting of Foreign Exchange Transactions to Trade Repository

RBI has issued a circular dated 8 November 2024 expanding the reporting requirements for foreign exchange (FX) transactions to the Trade Repository (TR) managed by the Clearing Corporation of India Ltd. (CCIL).

1. **Scope of reporting** – All foreign exchange contracts (hereinafter referred to as "FX contracts") are to be reported in a phased manner, including foreign exchange cash, foreign exchange tom and foreign exchange spot.
2. **Timelines** - Authorised Dealers (ADs) shall report all inter-bank FX contracts undertaken by them to the TR of CCIL with effect from 10 February 2025 as per the following timelines:
   1. Inter-bank FX contracts involving INR shall be reported in hourly batches within 30 minutes from completion of the hour. Such contracts executed 60 minutes prior to closure of CCIL's reporting platform for the day and subsequent to closure of CCIL's reporting platform for the day shall be reported by 10 a.m. of the following business day.
   2. Inter-bank FX contracts not involving INR executed up to 5 p.m. on any given day should be reported by 5:30 p.m. of that day. Such contracts executed after 5 p.m. should be reported by 10 a.m. of the following business day.
3. **Phased manner implementation** – ADs shall report all FX contracts executed with clients to the TR of CCIL in a phased manner as per the following timelines:
   1. FX contracts with the value equal to or exceeding the threshold limit of USD 1mn and equivalent thereof in other currencies with effect from 12 May 2025.
   2. FX contracts with the value equal to or exceeding the threshold limit of USD 50,000 and equivalent thereof in other currencies with effect from 10 November 2025
   3. FX contracts executed with clients should be reported before 12 noon of the following business day.
4. There shall be no requirement of matching transactions with overseas counterparties and client transactions in the TR as the overseas counterparties and clients are not required to report or confirm the transaction details.

This circular impacts all Authorised Dealers.

Operational Framework for Reclassification of Foreign Portfolio Investment to Foreign Direct Investment (FDI)

RBI *vide* notification dated 11 November 2024, has issued directions on Operational framework for reclassification of Foreign Portfolio Investment made by foreign portfolio investor along with its investor group (FPI) to Foreign Direct Investment (FDI).

As per Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (hereinafter referred to as 'Rules'), investments made by FPI shall be less than 10% of the total paid-up equity capital on a fully diluted basis. Any FPI breaching this limit shall either divested their holdings or reclassify such holdings as FDI subject to the conditions specified by the RBI and SEBI within 5 trading days (hereinafter referred as 'prescribed time') from the trade settlement date of settlement that caused the breach. Operational framework is prescribed in this notification for such reclassification, following are the key compliances:

1. **Necessary approval** - FPI shall obtain necessary approvals from the Government including for investments from land bordering countries and ensure compliance with FDI provisions such as entry route, sectoral caps, investment limits and pricing guidelines in the Rules.

   Further, FPI shall obtain concurrence of the Indian investee company concerned to ensure that such company also complies with conditions pertaining to sectors prohibited for FDI, sectoral caps, and government approvals under the Rules.
2. **Exclusions** - The reclassification option is not available for investments in sectors prohibited for FDI.
3. **Reporting to Custodian** - FPI shall notify its intent to reclassify its portfolio investment as FDI and provide the necessary approvals and concurrence to its Custodian and the Custodian shall freeze further equity purchase in the Indian company, till the reclassification is complete. If the necessary prior approvals/ concurrence are not obtained, then the investment beyond the prescribed limit shall be compulsorily divested within the prescribed time.
4. **Timely reporting -** For reclassification, the entire investment held by such FPI shall be reported within the timelines as specified under Foreign Exchange Management (Mode of Payment and Reporting of Non-Debt Instruments) Regulations, 2019.

These directions will become operative with immediate effect.

Securities and Exchange Board of India (SEBI)

Investments in Overseas Mutual Funds/ Unit Trusts by Indian Mutual Funds

SEBI issued a circular dated 4 November 2024, on Investments in Overseas Mutual Funds/ Unit Trusts (MF/UTs) by Indian Mutual Funds. As per SEBI master circular dated 27 June 2024, Mutual Funds are permitted to invest in overseas securities which also includes investment in overseas MF/ UTs. In order to facilitate ease of investment in overseas MF/ UTs, to bring transparency in the manner of investment, and to enable Mutual Funds to diversify their overseas investments, the following has been included in this circular:

1. **Limit on exposure to Indian securities** - Indian Mutual Fund schemes shall now invest in overseas MF/ UTs that have exposure to Indian securities, provided the total exposure to Indian securities does not exceed 25% of their assets.
2. **Breach of the limit** - Indian Mutual Fund schemes shall ensure at the time of an making investment (fresh or subsequent) that the underlying overseas MF/ UTs do not have more than 25% exposure to Indian securities. If this limit is breached, an observance period of six months from the date of publicly available information is allowed for monitoring portfolio rebalancing. During this period, the Indian Mutual Fund scheme cannot make any fresh investments in such overseas MF/ UTs and may resume their investments if the exposure to Indian securities by such overseas MF/ UTs falls below 25%.
3. **Rebalancing of portfolio** - If the underlying overseas MF/ UT does not rebalance its portfolio within the six-month observance period, Indian Mutual Fund scheme shall liquidate its investments in the overseas MF/ UT within the next six months (liquidation period). Further, failing to comply with rebalancing requirements, after the six-month liquidation period, the Indian Mutual Fund/ Asset Management Company shall not be permitted to accept fresh subscriptions, launch new schemes and levy exit load.
4. **Conditions for investment in overseas MF/ UTs** - SEBI has prescribed conditions for these investments, highlighted few below:
   - i. **Pooling** - All investor contributions in the overseas MF/ UT are pooled into a single investment vehicle with no side vehicles including segregated portfolios, sub-funds, or protected calls,.
   - ii. **Pari Passu and Pro-rata** – Corpus of the overseas MF/ UTs is a blind pool and all investors have pari-passu and pro-rata rights in the fund and share returns based their contribution.
   - iii. **No advisory agreements** – There shall be no such agreement between Indian Mutual Funds and the overseas MF/ UTs to prevent conflict of interest.

The provisions of this circular shall come into force with effect from the date of this circular.

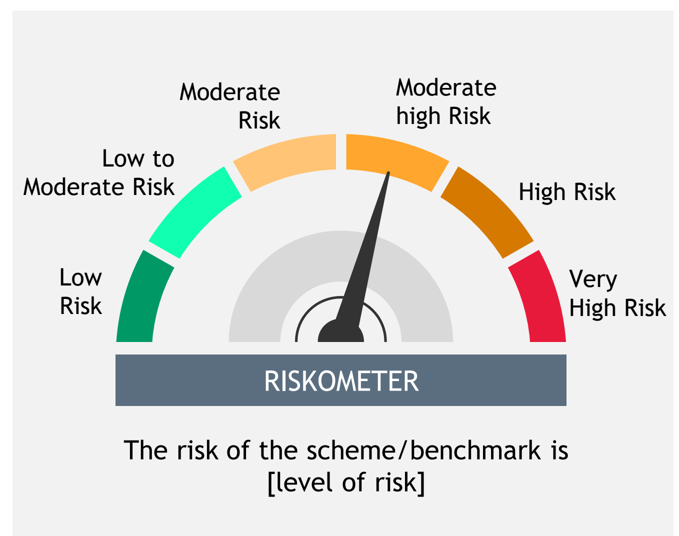
This circular impacts all Mutual Funds, all Asset Management Companies (AMCs), all Trustee Companies/ Boards of Trustees of Mutual Funds, Association of Mutual Funds in India (AMFI), and all Custodians.

Disclosure of Expenses, Half-yearly Returns, Yield, and Risk-o-Meter of Schemes of Mutual Funds

SEBI issued a circular dated 5 November 2024, introducing separate disclosure requirements for expenses, half yearly returns, yield of both direct and regular mutual fund plan along with colour coded risk-o-meter of schemes of Mutual Funds to improve transparency, make information easier for investors to understand and to standardise disclosures across Mutual Fund industry. Accordingly, following amendments have been introduced:

1. **Separate disclosure Requirements** - Investments under direct plan of a mutual fund scheme are not routed through distributors of mutual funds (MF). As no distribution expenses and commission are charged for direct plan, their expense ratios are lower than those of regular plans, leading to different returns between the two. Accordingly, the following disclosures are required:
   - i. Separate disclosures for total recurring expenses for direct and regular plans, along with total recurring expenses of the scheme, as per SEBI guidelines.
   - ii. Separate disclosures for returns during the half year and compounded annualised yields for direct and regular plans.

   To standardise these disclosures, the format for half-yearly financial statement for MF schemes shall be reviewed and finalised by Association of Mutual Funds in India (AMFI), in consultation with SEBI.
2. **Colour scheme for risk-o-meter** - Master Circular dated 27 June 2024 for Mutual Funds has been updated to include colour scheme for the risk-o-meter in addition to the existing risk levels. The revised risk levels and their corresponding colours are:



This colour scheme shall be applicable for all digital and polychrome printed promotion materials/ disclosures for the schemes.

3. **Disclosure of change in risk-o-meter -** Any change in the risk-o-meter shall be communicated to unitholders of that particular scheme by way of a Notice-cum-Addendum as well as an e-mail or SMS.

The provisions of this circular shall come into effect from 5 December 2024.

This circular impact all MF, Asset Management Companies (AMCs), all Trustee Companies/ Board of Trustees of Mutual Funds, all Registrar to an Issue and Share Transfer Agents (RTAs), and AMFI.

Advisory on Communication with SEBI Officials

SEBI has issued an advisory dated 7 November 2024 stating that various communications are received from registered intermediaries/ regulated entities seeking clarification on implementation of specific operational measures and/ or policy interpretation from time to time. However, communications which are in the form of a summary of discussions/ minutes of the meetings held with SEBI Officials or their understanding of the interpretation on a specific issue related to the securities markets shall not be considered as approval/ clarification from SEBI, unless the same is specifically communicated by SEBI.

Therefore, all registered intermediaries/ regulated entities are advised to implement measures requiring SEBI approval/ clarification from SEBI only after receiving explicit written approval or clarification from SEBI and refer to the mechanism provided for under the Securities and Exchange Board of India (Informal Guidance) Scheme 2003 (or any modification or re-enactment thereof) for seeking interpretive letters/ no action letters from SEBI, if required.

This Advisory is issued to all registered intermediaries/ regulated entities.

Relaxation from Certain Provisions for Units Allotted to an Employee Benefit Trust for the Purpose of a Unitbased Employee Benefit Scheme - Real Estate Investment Trusts (REITs)

SEBI vide circular dated 13 November 2024, issued following key amendments:

1. **Exemption from lock-in period** - In order to promote ease of doing business and to facilitate the acquisition of units by the employee benefit trust and the subsequent transfer of units to the employees, Master Circular for REITs dated 15 May 2024 has been amended to state that lock-in and allotment related restrictions contained in chapter 10 of this Master Circular shall not apply to the employee benefit trust.
2. **Standardisation of reporting formats -** To ensure uniformity across the industry, it has been stated that Indian REITs Association (IRA), in consultation with SEBI, shall specify the format of quarterly report and compliance certificate required to be submitted by the Manager of the REIT to the Trustee and publish it on its website.

This circular shall be applicable with immediate effect.

This circular impact IRA, all REITs, all Parties to REITs, all Recognised Stock Exchanges and all Depositories.

Relaxation from Certain Provisions for Units Allotted to an Employee Benefit Trust for the Purpose of a Unit-based Employee Benefit Scheme - Infrastructure Investment Trusts (InvITs)

SEBI issued a circular dated 13 November 2024, issued following key amendments:

1. **Exemption from lock-in period** - In order to promote ease of doing business and to facilitate the acquisition of units by the employee benefit trust and the subsequent transfer of units to the employees, Master Circular for InVITs dated 15 May 2024 has been amended to state that lock-in and allotment related restrictions contained in chapter 7 of this Master Circular shall not apply to the employee benefit trust.
2. **Standardisation of reporting formats -** To ensure uniformity across the industry, it has been stated that Bharat InvITs Association (BIA), in consultation with SEBI, shall specify the format of quarterly report and compliance certificate required to be submitted by the Manager of the REIT to the Trustee and publish it on its website.

This circular shall be applicable with immediate effect.

This circular impact BIA, all InvITs, all Parties to InvITs, all Recognised Stock Exchanges and all Depositories.

Master Circular for Compliance with the Provisions of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 by Listed Entities

SEBI has issued an updated Master circular dated 11 November 2024 for compliance with the provisions of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (SEBI LODR Regulations) by listed entities superseding erstwhile Master Circular dated 11 July 2023.

This updated Master Circular has incorporated circulars issued on or before 30 September 2024 and provides a chapter-wise framework for compliance with various obligations under the SEBI LODR Regulations.

All listed entities, recognised stock exchanges and depositories, and other stakeholders shall comply with the provisions of this circular to the extent applicable.

Master Circular for Issue of Capital and Disclosure Requirements

SEBI has issued an updated Master circular dated 11 November 2024, for compliance with the provisions of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements), 2018 (SEBI ICDR Regulations) by listed entities superseding erstwhile Master Circular dated 21 June 2023.

This updated Master Circular has incorporated circulars issued on or before 30 September 2024 and provides a chapter-wise framework for compliance with various obligations under the SEBI ICDR Regulations.

All Registered Merchant Bankers, Recognised Stock Exchanges, Depositories and Registered Depository Participants, Registered Registrars to an Issue and Share Transfer agents, Registered Stock Brokers, Registered Credit Rating Agencies, Bankers to an Issue (Self-Certified Syndicate Banks), Sponsor Banks, All listed entities/ proposed to be listed entities and National Payment Corporation of India (NPCI) shall comply with the provisions of this circular to the extent applicable.

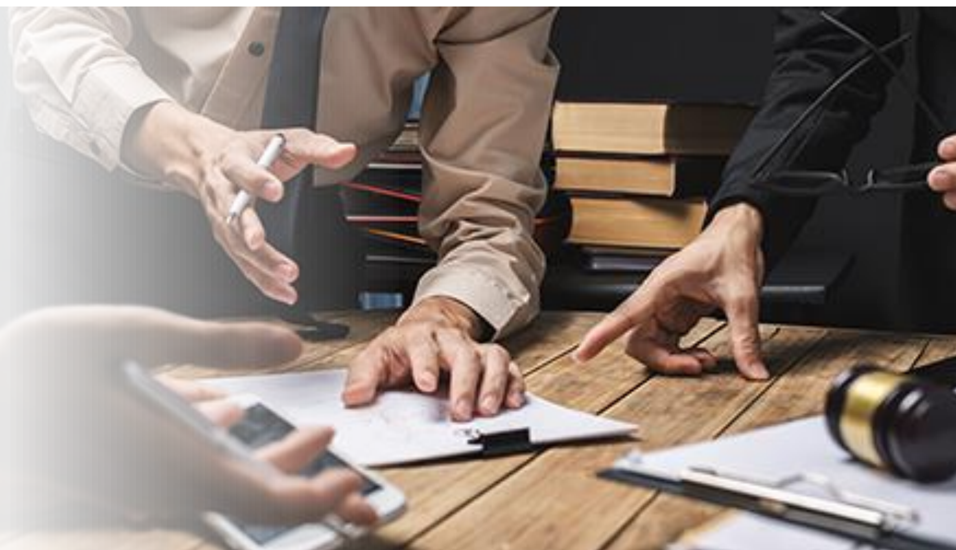
Securities and Exchange Board of India (Alternative Investment Funds) (Fifth Amendment) Regulations, 2024

SEBI *vide* notification dated 18 November 2024 has issued amendments to the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012. These Regulations may be called the Securities and Exchange Board of India (Alternative Investment Funds) (Fifth Amendment) Regulations, 2024.

Following are the key amendments made in Regulation 20 under General Obligations and Responsibilities and Transparency:

1. **Pro-rata rights of investors** - Investors in an Alternative Investment Fund (AIF) scheme shall have rights in each investment and its distribution of proceeds, proportional to their commitment to the scheme, unless specified otherwise by SEBI. However, rights of investors of AIF scheme issued prior to this notification, which are not exempted by SEBI and not proportional to their commitment to the scheme, shall be dealt in the manner specified by SEBI.
2. **Pari-Passu rights of investors** - Except for the rights mentioned above, investors in an AIF scheme shall have pari-passu rights in all aspects. However, differential rights may be offered to select investors as may be specified by the Board, without affecting the interest of other investors of the scheme. This provision of pari-passu rights shall not apply to Large Value Fund for Accredited Investors. Further, any differential rights already issued by an AIF before issue of this notification, shall be dealt in the manner specified by SEBI.

They shall come into force on the date of their publication in the Official Gazette.



REGULATORY UPDATES

REGULATORY UPDATES:

RESERVE BANK OF INDIA (RBI)

Notification No. RBI/2024-25/88 dated 7 November 2024 in connection with the Expansion of the Fully Accessible Route (FAR) for Non-Resident Investment by the inclusion of Sovereign Green Bonds

The FAR, initially introduced in 2020, allows non-resident investors to invest in specified Government of India securities without any investment ceilings. Reserve Bank of India (RBI) has expanded the scope of the FAR to allow non-residents to invest in Sovereign Green Bonds (10-year tenor) issued by the Government of India in the second half of fiscal year 2024-25. This aims to enhance global participation in India's green initiatives and aligns with the growing demand for sustainable investment opportunities.

This inclusion follows the RBI's Issuance Calendar for Marketable Dated Securities for October 2024 to March 2025, published in September 2024.

For more information, refer to the recent circulars issued by the RBI, including FMRD.FMSD.No.25/14.01.006/2019-20 and Subsequent updates.

These Directions shall be applicable with immediate effect.

SECURITIES AND EXCHANGE BOARD OF INDIA (SEBI)

Circular dated 11 November 2024: Procedure for reclassification of Foreign Portfolio Investors (FPI) investment to Foreign Direct Investment (FDI), (the Circular)

The Circular is addressed to FPI, Designated Depository Participants (DDPs), Custodians, Depositories, Stock Exchange and Clearing Corporations.

Earlier, under SEBI (FPI) Regulations, where an investor i.e. FPI's holdings exceed the prescribed threshold and where the FPI fails to divest its holding within five trading days, the entire investment including for the investment group will be reclassified as FDI.

The circular provided for the modified procedure and with immediate effect, to allow an FPI, or its investor group, to seek reclassification to FDI if their stake in the Investee company (Company) reaches 10% or more of the total paid-up equity capital of the Company on a fully diluted basis.

Upon receiving this intent from the FPI, the custodian is required to report to SEBI and freeze any further purchases of the Indian Company's shares, until the reclassification is complete as per Reserve Bank of India guidelines.

Once the above is completed, the Custodian to process the transfer of shares from the FPI demat to the FDI demat account.

Circular dated 11 November 2024: Trading supported by Blocked Amount in Secondary Market, (The Circular).

The Circular is addressed to all recognised Depositories, Stock Exchanges, Clearing Corporations and the National Payment Corporation of India.

In addition to the current mode of trading in the secondary market i.e. transferring funds directly to a Trading Member or broker, Qualified Stock Brokers (QSBs) now offer either of the below options to trade:

i. UPI-based block mechanism (i.e. Investors can block the necessary funds in their bank account. These funds will remain in the investor's bank account, but they will be unavailable for other use until the trade is completed.)

OR

ii. 3-in-1 trading account (i.e. It integrates a savings account, demat account, and trading account into a single, unified solution. This system allows investors to keep their funds in a savings account (earning interest), while their demat account holds their securities and the trading account facilitates transactions.)

Investors may choose to continue with an existing facility of trading or opt for either of the facilities stated above, as provided by QSB.

The Circular shall come into effect from 1 February 2025.

Circular dated 12 November 2024: Simplified registration for Foreign Portfolio Investors (FPIs), (the Circular)

The Circular is addressed to FPIs, Designated Depository Participants (DDPs), Custodians and Depositories and shall come into force after three months from the date of this circular.

Every FPI applicant is mandatorily required to submit a duly filled and signed Common Application Form (CAF) and Annexure to CAF along with documents for registration.

The Circular provides an option for certain categories of FPI (as mentioned in the Circular) to fill in the entire CAF or an abridged version of the CAF. Abridged CAF shall include only those fields which are unique to them and the remaining fields will be auto-populated from the CAF module or disabled.

Further, FPI shall provide explicit consent to use the pre-filled information and confirm that other details remain unchanged.

DDPs must update the CAF details in their systems and ensure the CAF module reflects complete information.

The standards for implementation and the fields that can be auto-populated or disabled will be formulated by the Custodians and Designated Depository Participants Standards Setting Forum in consultation with SEBI.

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Circular dated 18 November 2024: Amendment to Para 15 of Master Circular for Credit Rating Agencies (CRAs), (the Circular)

The Circular is addressed to registered CRAs, registered debenture trustees, recognised stock exchange, depositories and issuers who have listed and/or proposed to be listed securities, instruments or commercial papers.

Earlier, a delay of even one day or a shortfall of one rupee in repayment (principal or interest) from the scheduled date, was considered as default for debentures and bonds.

During the COVID-19 pandemic, SEBI introduced a provision for a 90-day post-default curing period. During this period, CRAs had a right to upgrade ratings from default to non-investment grade, on a case-by-case basis. Additionally, CRA were to frame a policy for upgrading the rating and include scenarios such as technical defaults, management changes, or significant financial inflows that alter the company's credit risk profile.

It was further suggested that CRAs should provide specific policy guidance on the treatment of 'technical defaults' in certain scenarios of non-payment of debt which are beyond the issuer's control, such as incorrect information, dormant investor account or government instructions to freeze the account of the investor.

Accordingly, to consider aforesaid scenarios, SEBI with immediate effect has now decided that CRAs shall:

i. Confirm and verify availability of funds, reasons for the failure, and ensure payments are made into an escrow account;

ii. Inform stock exchanges, depositories, and debenture trustees on the same day about the default, detailing the payment failure;

iii. Sensitise issuers to use measures like penny-drop verification or other suitable measures to prevent payment failures.

Consequently, the term 'technical default' has been removed from the Master Circular.

Circular dated 20th November 2024, The Securities and Exchange Board of India (SEBI) has introduced amendments to the Bankers to an Issue Regulations, 1994, through the Securities and Exchange Board of India (Bankers to an Issue) (Amendment) Regulations, 2024.

These amendments, which come into force on the date of their publication in the official gazette, expand the responsibilities of banks acting as intermediaries in securities issues.

Key changes include the addition of new services such as providing escrow services for issue management, buybacks, delisting and open offers. Banks will also be required to open separate accounts for depositing proceeds from initial or further public offerings.

Furthermore, the amendments introduce a registration requirement for entities wishing to act as bankers to an issue, mandating certification from SEBI. These changes aim to enhance the regulatory framework and increase accountability in capital market activities.

Circular dated 21 November 2024: Withdrawal of Master Circular on issuance of No Objection Certificate (NOC) for release of 1% of Issue Amount

Securities and Exchange Board of India (SEBI) has introduced amendments wherein the requirement for the issuer company to deposit 1% of the issue size with the stock exchange has been dispensed with i.e., it is no longer necessary for issuers to make this deposit when offering securities to the public.

Further, the Stock Exchanges are required to frame a joint standard operating procedure (SoP) for the release of a 1% security deposit that was deposited with stock exchanges by the issuer prior to the abovementioned amendments in ICDR Regulations, 2018.

The said change aims to make the process of doing business easier for issuer companies. The said circular shall be applicable with immediate effect.

Circular dated 26 November 2024: Valuation of repurchase (repo) transactions by Mutual Funds.

The Securities and Exchange Board of India (SEBI) has introduced amendments wherein in order to have uniformity in the valuation methodology of all money market and debt instruments and to address the concerns of unintended regulatory arbitrage that may arise, due to different valuation methodologies adopted, valuation of repurchase (repo) transactions including TREPS with tenor of upto 30 days will from now on be valued at mark to market basis as opposed to the earlier valuation method of cost plus accrual basis.

Further valuation of all repo transactions, except for overnight repos, in addition to the valuation of money market and debt securities, shall be obtained from valuation agencies. The provisions of the above-mentioned circular shall come into effect from 1 January 2025

Circular Dated 28 November 2024: SEBI introduces new guidelines to strengthen business continuity for interoperable segments of Stock Exchanges

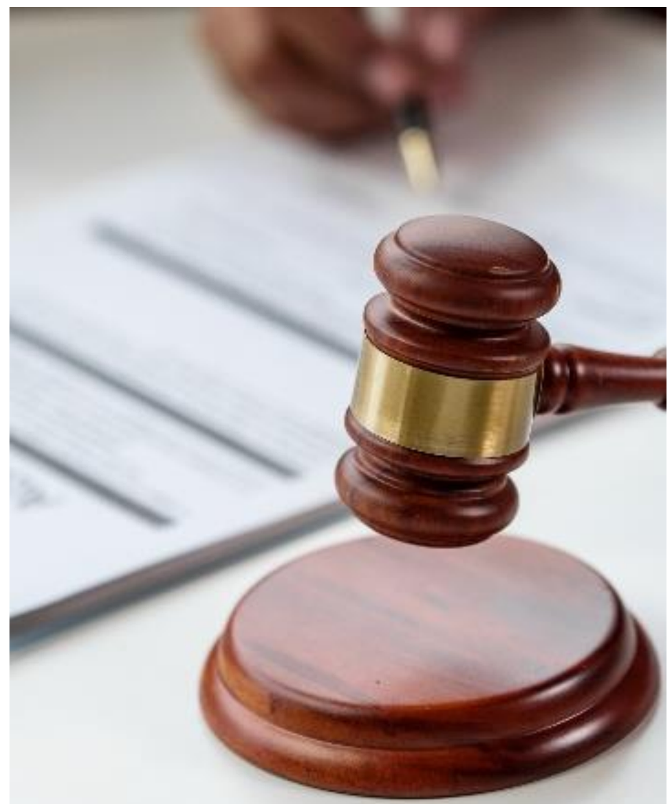
SEBI has introduced guidelines to enhance Business Continuity and Disaster Recovery systems for market infrastructure institutions, including stock exchanges (except commodity derivatives exchanges) and clearing corporations to ensure smooth functioning of the market during technical disruptions or emergencies.

The first phase of the framework was introduced in December 2023 and required Clearing Corporations to adopt a Software as a Service (SaaS) model for their Risk Management Systems.

The second phase focuses on mitigating risks from stock exchange outages during trading hours. If an outage occurs, market participants can hedge their positions on alternative exchanges through interoperability between exchanges and clearing corporations.

In case of an incident, the affected exchange must notify SEBI and the backup exchange within 75 minutes, and the backup exchange must activate its disaster recovery plan within 15 minutes. Initially, the NSE and BSE will serve as backup venues for each other, with a joint Standard Operating Procedure in place.

This circular will come into effect from 1 April 2025.



DIRECT TAX

CIRCULARS/ NOTIFICATIONS/ PRESS RELEASE

CBDT specifies monetary limits in respect of reduction or waiver of interest under section 220(2) of the IT Act

Section 220(2) of the Income-tax Act, 1961 (IT Act) deals with the consequences of non-payment of income tax by a taxpayer. If a taxpayer fails to pay the amount specified in the demand notice under section 156[1] of the IT Act, he shall be liable to pay simple interest at 1% per month or part of the month for the period of delay. In this context, Section 220(2A) of the IT Act empowers specified tax authorities for the reduction or waiver of such interest subject to the satisfaction of prescribed conditions.

The Central Board of Direct Taxes (CBDT) vide Circular has now specified monetary limits in respect of reduction or waiver of interest by the tax authorities as below:

S.NO.	TAX AUTHORITIES	MONETARY LIMITS
1.	Pr. CIT/ CIT	Upto INR 5mn
2.	CCIT/DGIT	Above INR 5mn to INR 15mn
3.	Pr. CCIT	Above INR 15mn

Further, reduction or waiver of interest under section 220(2) of the IT Act shall continue to be subject to satisfaction of all conditions outlined below:

(i) Payment of such amount has caused or would cause genuine hardship to the taxpayer;

(ii) Default in payment on which interest has been paid or was payable was due to circumstances beyond the control of the taxpayer; and

(iii) The taxpayer has co-operated in any inquiry relating to the assessment or any proceeding for the recovery of any amount due from him.

This Circular is applicable from the date of its issue.

[Circular No. 15/2024, dated 4 November 2024]

CBDT issues FAQs on the PAN 2.0 Project

The Cabinet Committee on Economic Affairs (CCEA) has approved the Income Tax Department's (ITD) PAN 2.0 Project (PAN 2.0). PAN 2.0 aims to streamline and modernise the process of issuing and managing Permanent Account Number (PAN) and Tax Deduction and Collection Account Number (TAN) and making it more user-friendly and efficient.

Currently, PAN-related services are spread across three different platforms: the e-Filing Portal, UTIITSL Portal, and Protean e-Gov Portal. With the implementation of PAN 2.0, all these services will be integrated into a single, unified portal. This one-stop platform will handle comprehensive issues related to PAN and TAN, including application, updates, corrections, Aadhaar-PAN linking, re-issuance requests and online PAN validation.

Key features of PAN 2.0:

- Single portal for all PAN/TAN-related services to simplify access for users.
- Eco-friendly paperless processes to reduce paperwork.
- PAN will be issued free of cost with quicker processing times.
- Personal and demographic data will be protected through enhanced security measures, including PAN Data Vault.

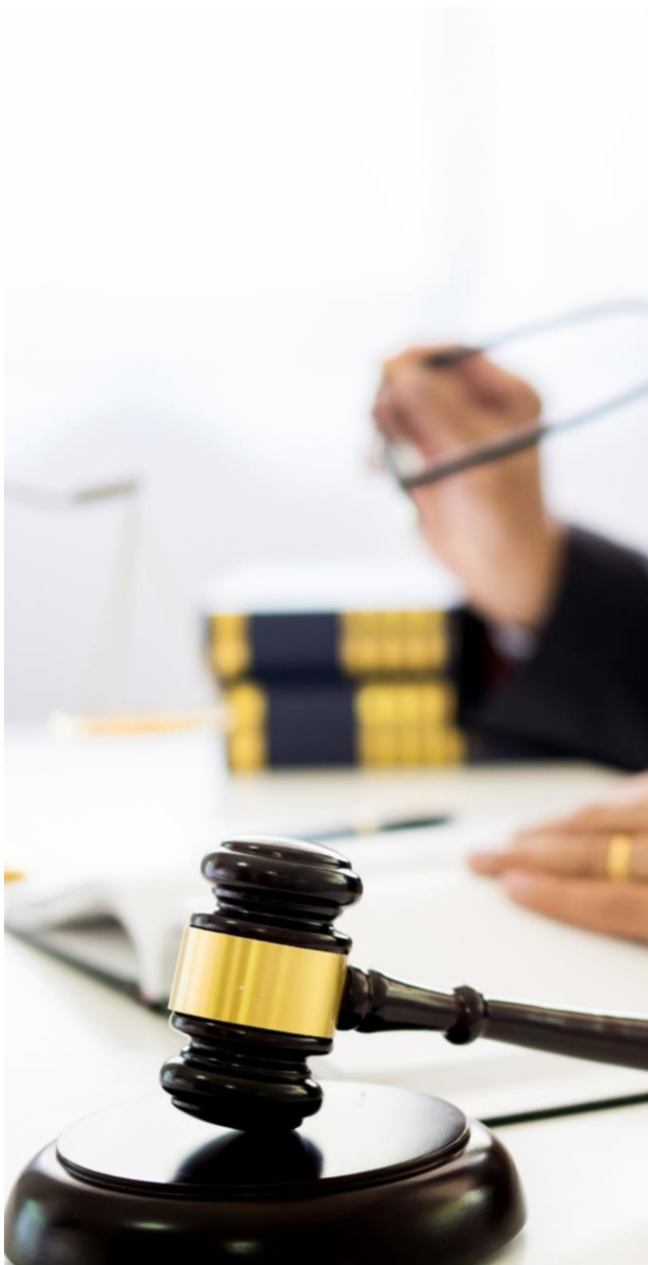
[1] Section 156 of the IT Act provides for notice of demand when any tax, interest, penalty, fine or any other sum is payable in consequence of any order passed under the IT Act.

- Dedicated call centre and helpdesk to address user queries and issues.

Additionally, to provide clarity, the CBDT has issued FAQs in an easy-to-understand manner and the key FAQs are listed below:

- How PAN 2.0 will be different from the existing setup?
- Whether existing PAN card holders will be required to apply for new PANs under the upgraded system?
- Do existing PAN card holders need to change their PAN or PAN cards under PAN 2.0?
- If new PAN cards are QR code enabled, will older ones continue to function as it is?
- For taxpayers holding more than one PAN, how will extra PANs be identified and weeded out?

[CBDT Press Release dated 26 November 2024]



JUDICIAL UPDATES

Hyderabad Tax Tribunal holds that benefit under section 115BAB of the IT Act to be granted if the taxpayer proves commencement of manufacturing activities in subsequent FY and should not act upon the earlier Form

Taxpayer, an Indian company set up in January 2023 had filed its return of income for Fiscal Year (FY) 2022-23 along with Form 10-ID and claimed the benefit of concessional tax regime under section 115BAB of the IT Act. The tax officer denied this claim since the taxpayer had not commenced manufacturing/ production during the year under consideration. Aggrieved, the taxpayer filed an appeal before the First-Appellate Authority which was dismissed on the ground that the main condition for claiming benefit under section 115BAB of the IT Act was not satisfied since no manufacturing had taken place during the year. Further aggrieved, the taxpayer filed an appeal before the Hyderabad Tax Tribunal which made the following observations while ruling in favour of the taxpayer:

- Section 115BAB of the IT Act clearly postulates that a company must have been set up on or after 1 October 2019 and commenced manufacturing or production of an article or thing on or before 31 March 2024.
- Form 10-ID provides that any new manufacturing domestic company can opt to pay tax at a concessional tax rate of 15% under section 115BAB of the IT Act subject to certain conditions. It is essential to file Form 10-ID on or before the due date for furnishing the return of income for the first Assessment Year (AY) commencing on or after the first day of April 2020 to avail of such benefit.
- In the present case, the first AY corresponds to FY 2022-23 and Form 10-ID is filed prior to the commencement of manufacturing activities. In this context, the taxpayer cannot be expected to file Form 10-ID, showing the commencement of manufacturing activities when the date of commencement of manufacturing activity was allowed up to 31 March 2024 as per Section 115BAB of the IT Act.
- Also, FAQs on Form 10-ID clearly provide that the taxpayer is not required to file a fresh Form 10-ID after filing it for the first AY. Therefore, the contradiction is clear that even if the taxpayer had not commenced manufacturing activities, it was required to file a certificate showing the commencement of such activities and it was prohibited to file Form 10-ID in subsequent years when manufacturing activities actually commenced.
- In view of the above harmonious interpretation, though manufacturing activities had not commenced during the year under consideration i.e. FY 2022-23 when the taxpayer started its manufacturing activities, the same should be factored for the purpose of a concessional tax regime.

- Although the issue pertains to FY 2022-23, assessment is a continuous process and denial of benefit for year under consideration would affect the subsequent year as no fresh Form 10-ID can be filed. Hence, if the taxpayer can prove the commencement of manufacturing activities in subsequent FY (i.e. FY 2023-24), the benefit of a concessional tax regime for subsequent FYs should be granted.

[Granules CZRO Private Limited Vs ITO, I.T.A. No. 706/Hyd/2024 (Hyderabad Tax Tribunal)]

Reassessment under section 147 of the IT Act can be initiated if the tax officer does not assume jurisdiction under section 153C of the IT Act due to non-fulfilment of jurisdictional conditions.

The taxpayer was engaged in the business of trading shares, securities, commodities, etc. A search was conducted under section 132[2] of the IT Act on two persons and the seized documents revealed that the taxpayer was a major beneficiary of accommodation entry in respect of operations carried on by these two persons. Further, the tax officer had also received information from the Investigation wing that the taxpayer had purchased units of penny stock. Based on the information and material available, the tax officer issued a notice under section 148[3] of the IT Act after prior approval from the competent authority. The taxpayer contended that recourse to section 147[4] of the IT Act would not be available in cases where the tax officer is empowered to proceed under section 153C[5] of the IT Act. However, the taxpayer's income was reassessed and the assessment order passed accordingly under section 147 of the IT Act.

Aggrieved, the taxpayer filed an appeal before the First-Appellate Authority which was dismissed. Further aggrieved, the taxpayer filed an appeal before the Delhi Tax Tribunal which was allowed on the grounds that the tax officer was required to frame the reassessment under section 153C of the IT Act and was precluded from proceeding under section 147 of the IT Act. Aggrieved, the tax officer filed an appeal before the Delhi High Court. The principal issue was the interplay between the provisions of sections 153C and 147 of the IT Act. The Delhi High Court made the following observations while deciding the issue in favour of the tax authorities:

- The taxpayer's contention was based essentially on two grounds. First, the provisions of section 153C of the IT Act are special provisions relating to assessment pursuant to material found during the search operations conducted on another person and hence, the same would override the provisions of section 147 of the IT Act. Second, section 153C of the IT Act commences with a non-obstante provision with the words "notwithstanding anything contained in sections 139, 147, 148, 149[6],151[7] and 153[8] of the IT Act". Hence, the taxpayer contended that the provisions of section 147 of the IT Act are overridden by the provisions of section 153C of the IT Act in cases where the reassessment is based on information or material found during a search.
- In case of a search conducted on a person (searched person) and assets, documents or books of account, pertaining to another taxpayer are found and handed over to a tax officer (of other than a searched person), it would be subject to satisfaction of other jurisdictional conditions under Section 153C of the Act. Having jurisdiction to make a reassessment/ assessment of taxpayer under Section 153C of the Act, does not mean that tax officer is bound to exercise said jurisdiction. In the event, that the tax officer does not assume its jurisdiction to proceed with making an assessment/ reassessment under Section 153C of the Act, recourse to Section 147/148 of the IT Act is not ousted.
- The non-obstante provision kicks in only when the tax officer assumes jurisdiction under Section 153C of the Act i.e. if such tax officer exercises its jurisdiction to initiate the machinery provisions of Section 153C of the Act to make an assessment/ reassessment of the taxpayer's income. The non-obstante provisions do not come into play if the tax officer does not take recourse to Section 153C of the IT Act.

[PCIT Vs Naveen Kumar Gupta, I.T.A. No. 401/2022 (Delhi High Court)]

[2] Section 132 of the IT Act empowers the tax authorities to conduct search and seizure operations.
[3] Section 148 of the IT Act provides for the issue of notice where income has escaped assessment.
[4] Section 147 of the IT Act provides for assessment/reassessment of income if it has escaped assessment.
[5] Section 153C of the IT Act provides for the assessment/reassessment of income of a person other than the person in whose case the search has been conducted.
[6] Section 149 of the IT Act provides the time limit for issue of notices under sections 148 and 148A of the IT Act.
[7] Section 151 of the IT Act specifies the competent authority for sanctioning the issue of notices under sections 148 and 148A of the IT Act.
[8] Section 153 of the IT Act provides the time limit for completion of assessment, reassessment and recomputation of income.

INDIRECT TAX

Quashes Validity of the Press Release Determining the Classification of Hand-sanitiser as ‘Disinfectant’

Schulke India Pvt. Ltd. vs. Union of India and Ors. [TS-727-HC(BOM)-2024-GST]

Facts of the Case

- M/s. Schulke India Pvt. Ltd. (Taxpayer) is engaged in trading of hand rubs/ sanitisers and antiseptics that are used as pharmaceutical aid (solvent) or as antibacterial/ antisepsis solutions in hospitals. Accordingly, these products were sold as a ‘medicament’ (HSN 3004) under the erstwhile Central Excise/ VAT laws as well as the GST law.
- The Ministry of Finance (MoF) issued a Press Release dated 15 July 2020 (Impugned Press Release) purporting to classify alcohol-based hand sanitisers as ‘disinfectants’ attracting GST @ 18%.
- Basis the Impugned Press Release, the tax authorities had issued a show cause notice to the Taxpayer (Impugned SCN) alleging that alcohol-based hand rubs/ sanitisers and antiseptics were not ‘medicaments’ but were ‘disinfectants’ attracting GST @ 18%.
- Subsequently, the Taxpayer paid the differential GST under protest and challenged the Impugned Press Release and the Impugned SCN *vide* the present Writ Petition before the Bombay High Court.

Contentions of the Taxpayer

- The Impugned Press Release is manifestly arbitrary and without the authority of law since the issue as to whether the products supplied by Taxpayer constitutes ‘medicament’ or ‘disinfectant’ is an issue that can be adjudicated by judicial and quasi-judicial authorities and not by MoF.
- Even if it is assumed that the Impugned Press Release is relatable to Article 73 of the Constitution of India (Constitution), it transgresses the limits imposed by the doctrine of separation of powers.
- The Impugned Press Release tends to foreclose fair adjudication by tax authorities in discharging their judicial/ quasi-judicial functions. Reliance was placed on various judicial precedents[1].
- On 21 September 2020, the Directorate General of Health Services had clarified that hand sanitisers for external use are covered under the definition of ‘Drug’ as per the Drugs and Cosmetics Act, 1940 (DC Act), hence, it cannot be classified as a ‘disinfectant’ or a ‘cosmetic’. Since two departments of Union of India should not be allowed to take contradictory pleas, the Impugned Press Release, and consequently, the Impugned SCN are liable to be set aside.
- Notification dated 27 July 2020 issued by the Ministry of Health and Family Welfare provides that hand sanitisers are drugs under DC Act and hence, exempted from licensing requirement for sale.
- Reliance was also placed on ***Reckitt Benckiser India Ltd. Vs. CCT [2023 (384) ELT 616 (SC)]*** where the Supreme Court had classified ‘Dettol antiseptic liquid’ as ‘medicament’ under HSN 3004. In the present case, since product under consideration was not different, the Impugned Press Release and the Impugned SCN are liable to be quashed and set aside.

[1] Parle Agro Pvt. Ltd. Vs. Union of India [2023 (12) Centax 199 (Mad.)], Association of Technical Textiles Manufacturers and Processors Vs. Union of India [2023 (12) Centax 195 (Del.)] and Phonographic Performance Ltd. Vs. State of Goa and Ors. [2024 SCC OnLine Bom 2713]

Contentions of the Tax Authorities

- The Writ Petition is not maintainable in the present case because adjudication of the Impugned SCN is yet to be completed. Further, even if after adjudication, the tax demand is confirmed, the Taxpayer has the remedy of statutory appeal.
- Relying on dictionary definitions, statutory provisions and precedents, the products under consideration are not 'medicaments' but are 'disinfectants' and hence, attract GST @ 18%.
- The Impugned Press Release is an executive instruction under Article 73 read with Article 77 of the Constitution. Since the Impugned Press Release is not contrary to statutory provisions, it must be given effect as guidance to tax authorities to levy correct GST on alcohol-based hand sanitisers.
- An executive action which is not contrary to any provision of the Constitution/ Statute is *intra vires* and hence, enforceable. Reliance was placed on various judicial precedents[2].
- Hence, Union of India, by exercising its executive powers was entitled and empowered to issue the Impugned Press Release. Further, since the same was not contrary to but consistent with applicable legal provisions, there was no infirmity in issuing either the Impugned Press Release or the Impugned SCN.

Observations and Ruling of the High Court

- The issue pertaining to the classification of the hand sanitisers i.e., whether as 'medicament' or as 'disinfectant' will have to be decided by the adjudicating authority because its adjudication would involve examination into disputed factual aspects. The issue in the present case is restricted to the validity of the Impugned Press Release since the adjudicating authority may not be able to decide on the validity or otherwise of the Impugned Press Release.
- The Impugned Press Release does not indicate that the same is related to either Article 73 or Article 77 of the Constitution. Although this by itself may not be a ground to strike down the Impugned Press Release, nonetheless, in the absence of any such indication/ compliance with Article 77 of Constitution, it cannot be accepted that the Impugned Press Release is an instance of the exercise of executive power by the Union of India.
- Assuming that the Impugned Press Release is an instance of exercising the executive power, it cannot be accepted that Union of India is empowered to direct judicial/ quasi-judicial authorities to decide the issue of classification because the same is essentially an interpretational issue that must be undertaken by judicial/ quasi-judicial authorities under the statute.
- The Legislature cannot simply issue a Press Release to explain, *post facto*, what it meant or intended to do when it enacted the law. What even a legislature could not possibly do, cannot be done by Union purporting to exercise its executive powers under Article 73 of Constitution. The executive power of the Union will extend to matters with respect to which Parliament is empowered to make laws and the same is only co-extensive with the Union's legislative powers.
- If the Parliament becomes *functus officio* when it comes to interpretation of law made by it, without undertaking the whole process of law-making, the Union, in exercise of its executive powers cannot claim some powers which transgresses the powers of the Parliament.
- The issue pertaining to the classification of a product after the law is enacted and classification is made, falls within the province of judicial/ quasi-judicial authorities and the same must be exercised independently and without any goading from any party, including the executive.
- Although *prima facie* the clarification and the notification relied upon by the Taxpayer indicates that the departments of the Union have accepted that hand sanitisers are 'drugs' and not mere 'disinfectants', the same was not deliberated upon since the same would be determined by the tax authorities based on facts and without being influenced by the Impugned Press Release that is proposed to be set aside.
- In view of the above, the Impugned Press Release is set aside with a direction that if the Impugned SCN is to be pursued, the tax authorities must decide the same as per law on its own merits without even remotely being influenced by the Impugned Press Release.

[2] Rai Sahib Ram Jawaya Kapur and Ors. Vs. State of Punjab [AIR 1955 SC 549] and Bengal Iron Corporation and Anr. Vs. Commercial Tax Officer and Ors. [1994 Supp (1) SCC 310]

Allows Credit of IGST Credit Availed as CGST and SGST

Rejimon Padickapparambil Alex vs. Union of India and Ors. [TS-781-HC(KER)-2024-GST]

Facts of the Case

- Rejimon Padickapparambil Alex (Taxpayer), running a proprietorship concern under the trade name 'Padiken Silks', is a registered person in Kerala under the Central Goods and Services Tax Act, 2017 (CGST Act).
- During the period from July 2017 to March 2018, the Taxpayer had received supplies from outside the State of Kerala on which the supplier had charged IGST. However, the Taxpayer, instead of taking input tax credit (ITC) of IGST paid on such procurements in Form GSTR-3B, had inadvertently showed the IGST component as Nil and added the bifurcated CGST and SGST components of such credit to the existing figures of eligible CGST and SGST credits. This had resulted in mismatch between Form GSTR-2A vis-à-vis Form GSTR-3B. However, it is undisputed that it was the amount of IGST credit (as appearing in Form GSTR-2A) that was split into the components of CGST and SGST and added to the corresponding fields in Form GSTR-3B.
- On observing the above mismatch, tax authorities issued a show cause notice (SCN) demanding CGST and SGST amounts alleged utilised in excess by the Taxpayer. The aforesaid SCN culminated in the issuance of the order (Impugned Order) confirming the demand against the Taxpayer.
- Against this, the Taxpayer filed a Writ Petition before the Kerala High Court wherein the High Court observed that the Taxpayer had by way of abundant caution also sought refund of ITC available with the tax authorities consequent to payment of IGST by the supplier and consequently, merely directed the tax authorities to consider and pass orders on the refund application without pronouncing on the legality of the actions of the tax authorities.
- Aggrieved by the above, the Taxpayer filed an appeal before the Division Bench of the High Court.

Contentions of the Taxpayer

- The Impugned Order was wholly unsustainable since there was admittedly no excess utilisation of ITC since the Taxpayer was entitled to take ITC of IGST paid on procurements.
- The only mistake that was occasioned by the Taxpayer was that he had not shown the IGST amount separately and had resorted to an exercise of splitting the same towards CGST and SGST on the premise that the Taxpayer did not have any outward supply attracting IGST liability.
- Reliance in this regard was also placed on the order passed by the Assistant Commissioner of Central Tax, Bengaluru (OIO) involving identical facts wherein the tax authority had *inter alia* observed that since there was no loss of revenue, either to the Centre or to any State arising from availment of CGST/ SGST instead of IGST, the assessee was not liable to reverse CGST and SGST availed on the procurements.

Observations and Ruling of the High Court

- The OIO not only represents the correct view of the procedural law but also demonstrates that the tax authorities even at the level of Assistant Commissioner are capable of rendering timely and effective justice in our country which is known for huge backlog of cases.
- An expeditious disposal of cases, especially those involving procedural aspects of taxation is the need of the hour so as to ensure fairness and certainty in tax administration.
- In the present case, the demand confirmed against the Taxpayer were in the proceedings initiated under Section 73 of the CGST Act that is attracted only when it appears to a proper officer that any tax has not been paid or short paid or erroneously refunded or where ITC has been wrongly availed or utilised for any reason. In the present case, there has been no wrong availment of ITC and the only mistake committed by the Taxpayer was an inadvertent and technical one where he had omitted to mention IGST figures separately. The mistake was also insignificant because it was undisputed that there was no outward supply attracting IGST liability.
- In view of the above, the judgement passed by the Single Judge of the High Court was set aside and the Writ Petition was allowed by quashing the Impugned Order and declaring that the Taxpayer shall not be seen as having availed excess ITC for initiating proceedings under Section 73 of the CGST Act.
- As regards the apprehension of the tax authorities that the State might be deprived of its legitimate share of IGST paid by suppliers outside the State, it was directed that when the State of Kerala produces the copy of the High Court judgement along with a representation before the GST Council, the GST Council must issue necessary directions to resolve the issue by taking note of the declaration in this judgement.

Allows Negative Blocking of ITC under Rule 86A of the CGST Rules

Tvl. Skanthaguru Innovations Pvt. Ltd. vs. Commercial Tax Officer and Ors. [TS-793-HC(MAD)-2024-GST]

Facts of the case

- Against Tvl. Skanthaguru Innovations Pvt. Ltd. (Taxpayer), the following proceedings were initiated by the Central Tax Authorities (CT officers):
  - Search was conducted and it was observed that till March 2024, the Taxpayer had wrongfully availed ITC of INR 63mn.
  - Accordingly, CT officers issued summons and the statement of the one of the Taxpayer's Directors was recorded. Later, the Director was arrested, and the Taxpayer's bank accounts were frozen. Subsequently, the arrested Director was released on bail.
  - Pursuant to the above, the Taxpayer paid a sum of INR 13mn as GST to demonstrate its *bona fide* intention and consequently, the attachment order (*qua* bank accounts) was lifted.
- Subsequent to the above proceedings initiated by the CT officers, the State Tax Authorities (ST officers) passed three separate orders for blocking the Taxpayer's Electronic Credit Ledger (ECL) to the tune of INR 24.8mn. However, at the time of issuing the said order, the amount available in ECL was Nil.
- When ECL was initially blocked *vide* the first order for INR 0.07mn, the Taxpayer had admitted the said tax dues in another proceeding with the CT officer and the matter had attained finality.
- Subsequently, without considering the finality of the above matter before the CT officer, the ST officers had issued notice in form GST ASMT-10 pertaining to the period till September 2024 alleging wrongful availment of ITC of INR 131.4mn. Later, the CT officers issued Form GST DRC-01A to the Taxpayer to the tune of INR 131mn.
- Aggrieved by the above, the Taxpayer filed a Writ Petition before the Madras High Court *inter alia* raising the following questions of law:
  - Whether ST officers are empowered to issue Form GST ASMT-10 subsequent to the search conducted by CT officers
  - Whether blocking of ITC is in accordance with Rule 86A of the Central Goods and Services Tax Rules, 2017 (CGST Rules)
  - Whether issuance of Form GST DRC-01A pertaining to INR 0.07mn and remitting the said amount in Form GST DRC-03 and dropping of proceedings amounts to determination of the entire issue in Form GST ASMT-10

Contentions of the Taxpayer

- The ST officers do not have any concurrent jurisdiction since the CT officers have already initiated proceedings for the very same issue by conducting search at the Taxpayer's premises.
- As per Rule 86A of the CGST Rules, in order to block ECL, credit should be available in the ECL at the time of blocking. If there is 'Nil' balance in ECL, there cannot be any negative blocking of credit since the same is impermissible. Reliance in this regard was placed on ***Samay Alloys India Pvt. Ltd. Vs. State of Gujarat [2022 (61) GSTL 421 (Guj.)]*** and ***Best Crop Science Pvt. Ltd. Vs. Principal Commissioner, CGST Commissionerate [2024 (22) Centax 531 (Del.)]***.
- The ST officer should record the reasons to believe that ITC has been fraudulently availed by the Taxpayer and the same is ineligible. In the present case, when the ECL was initially blocked for INR 0.07mn, the Taxpayer had admitted the said tax dues (in another proceeding with the CT officer) and the matter had attained finality. However, without considering the proceedings initiated by the CT officers, the ST officer had also initiated similar proceedings and issued Form GST ASMT-10.
- The ST officers will not have jurisdiction when the CT officer has already initiated proceedings on the same issue and has issued Form GST DRC-01A, Form GST ASMT-10, and ECL blocking orders issued by ST officers must be quashed.

Contentions of the Tax Authorities

- Initially, CT officers had initiated proceedings pertaining to the period till March 2024 for wrongful availment of ITC to the extent of INR 6mn. However, the ST officers have found that the wrongful utilisation of ITC for the period till September 2024 is INR 131mn. Although the issues are similar in nature, the quantum of amount and period pertaining to initiation of proceedings for wrongful availment of ITC by CT officers and ST officers are entirely different.
- If the Taxpayer is aggrieved over the aspects with regard to the quantum of amount and double prosecution, they can very well file their reply in which case the tax authorities would have certainly considered the same and dropped the proceedings accordingly.
- As on the date of issuance of Form GST ASMT-10, no proceedings were initiated by the CT officers for wrongful availment of ITC to the tune of INR 131mn. Hence, the Taxpayer cannot take a stand that ST officers do not have any authority to initiate proceedings for the quantum of amount which was wrongly availed by the Taxpayer.
- Considering that the CT officer has issued Form GST DRC-01A to the extent of INR 131mn, if any further orders are issued on the same issue by the ST officers, the Taxpayer can challenge the same before the High Court. However, the present Writ Petition filed by the Taxpayer is premature.
- The ST officers alone are empowered to pass blocking orders since the Taxpayer is allotted to the State jurisdiction. As per the settled position, once any wrongful availment of ITC comes to the knowledge of the ST officers, though the jurisdiction was already exercised by CT officers, the ST officers would still be empowered to issue blocking orders to protect State's revenue. Hence, the issue pertaining to concurrent jurisdiction for initiation of proceedings cannot be linked with blocking of ECL.

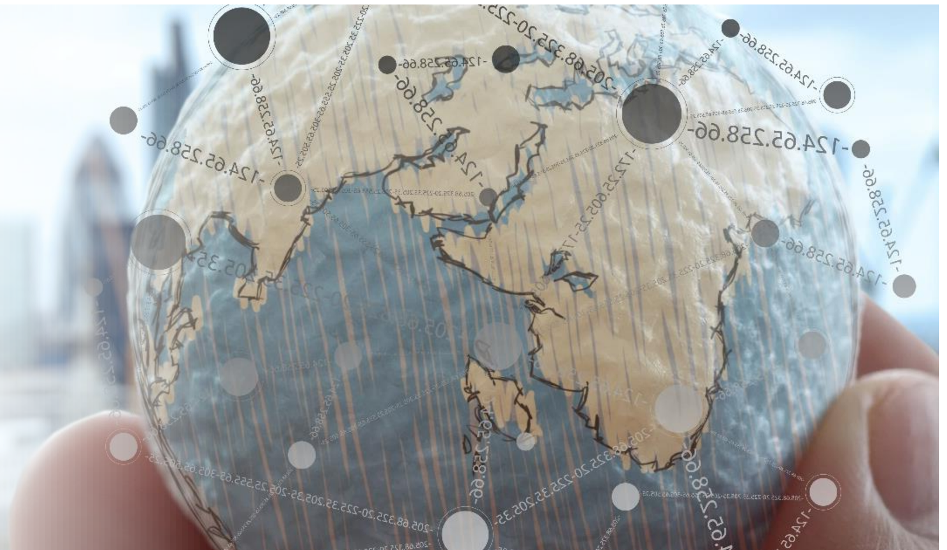
Observations and Ruling of the High Court

- **Whether ST officers are empowered to issue Form GST ASMT-10**:
  - Though the issue raised by the CT officers and the ST officers is similar, the quantum of amount demanded by them are entirely different and the period of demand also differs. Thus, the question of cross-empowerment would not arise.
  - As a result, to the extent of difference in amount and period, the ST officers will have the power to issue Form GST ASMT-10 and hence, the ST officers will certainly have the power to impose further prosecution for the issues which are left out by the CT officers.
  - Since at the time of issuance of Form GST ASMT-10, only search was conducted and no notice was issued by CT officers with regard to wrongful availment of ITC, one cannot assume or presume that the issue of cross-empowerment will come into picture against the ST officers.
  - Given that now the CT officer has issued form GST DRC-01A with regard to wrongful availment of ITC till September 2024 for INR 131mn, the ST officers certainly cannot proceed based on Form GST ASMT-10. In the absence of any further orders, subsequent to the issuance of Form GST ASMT-10 by ST officers, it is premature to decide as to whether ST officers are barred by cross-empowerment for initiation of proceedings against the Taxpayer.
  - However, blocking of ITC will always be the domain of ST officers, as accepted by CT officers, considering that the Taxpayer is registered under the jurisdiction of ST officers.
  - Though the issues raised by CT officer and ST officers are similar, if the period for which the notice was issued is different, both the authorities are empowered to initiate proceedings for the respective period. Consequently, the ST officers have acted well within their power/ jurisdiction, and it is premature to conclude as to whether the cross-empowerment will come into picture or not.
- **Whether blocking of ITC is in accordance with Rule 86A of CGST Rules**:
  - To interpret Rule 86A of CGST Rules, the said rule can be bifurcated into the following parts:
    - **First part**: The first part states that if Commissioner/ Assistant Commissioner has reason to believe that ITC available in ECL is fraudulently availed or is ineligible, the said ECL can be blocked under the circumstances mentioned in Rule 86A(1)(a) to (d) of CGST Rules.
    - **Second part**: The second part provides that the officer has to record reasons in writing not to allow the debit of the amount equivalent to such credit for discharge of liabilities under Section 49 of CGST Act.
  - A conjoint reading of the above would reveal that the phrase '***credit of ITC available in the ECL***' referred to in the first part would mean that the amount available after the fraudulent availment of ITC at any point of time, whether it was available in the ECL or utilised at the time of passing the blocking orders. Hence, the second part empowers the tax authorities not to allow debit of the amount equivalent to the fraudulently availed ITC for discharging liabilities.
  - If ITC was already utilised, the tax authorities are empowered to pass blocking orders to the extent of amount equivalent to such ITC which was already utilised along with the unutilised fraudulently availed ITC available in ECL at the time of passing blocking orders.
  - In ***Samay Alloys (supra)*** and ***Best Crop Science Pvt. Ltd. (supra)***, the High Courts have only taken into consideration the first part and hence, absent consideration of the second part of Rule 86A of CGST Rules, these rulings cannot be relied upon.

- Rule 86A of CGST Rules nowhere prohibits negative blocking of ITC. If the intention of the legislature is not to allow negative blocking, the same should have been specifically prohibited by virtue of a *proviso* or otherwise. In the absence of such prohibition, the blocking of ITC under Rule 86A of CGST Rules has to be construed for both positive and negative blocking and hence, the question of barring negative blocking would not arise.
- Thus, to the extent of utilisation of fraudulently availed ITC, ST officers are empowered to pass blocking orders for payment of output liabilities. In the present case, although the ST officers were empowered to pass blocking orders to the extent of INR 131mn, they had only blocked INR 24.8mn.
- In view of the above, negative blocking is well within the scope of Rule 86A of CGST Rules and the ST officers are empowered to pass the blocking orders up to the maximum extent of INR 131mn which was fraudulently availed and available in ECL for discharging output liabilities either at the time of blocking or subsequently, even if the same was already utilised.

- **Whether issuance of Form GST DRC-01A pertaining to INR 0.07mn and remitting the said amount and dropping of proceedings amounts to determination of the entire issue in Form GST ASMT-10:**
  - The payment of INR 0.07mn relates to the blocking of ITC under Rule 86A of CGST Rules in one of the orders whereas Form GST ASMT-10 was issued by ST officers for INR 131mn. As regards the other issues, the ST officers are yet to initiate proceedings. However, due to the subsequent development of issuance of subsequent blocking orders and the issuance of Form GST ASMT-10 by ST officers, for the remaining issues, the ST authorities are empowered to initiate proceedings.
  - Given that the CT officer has issued Form GST DRC-01A pursuant to the issuance of Form GST ASMT-10 by the ST officers, it is for the ST officers to decide as to whether all the issues pertaining to Form GST ASMT-10 issued by them are covered by Form GST DRC-01A, for which, the Taxpayer has to file reply. Upon considering the said reply, the ST officers has to consider the same and decide with regard to the continuation of the proceedings.

As a result, the submissions made by the Taxpayer are rejected and the writ petition is dismissed.



TRANSFER PRICING

Special Bench (SB) of Hon'ble Tax Tribunal, Ahmedabad: rules transaction between a foreign enterprise and its Indian PE is an international transaction subject to the application of transfer pricing provisions

TBEA Shenyang Transformer Group Company Limited (TBEA China/ HO), incorporated in and tax resident of China, was awarded a contract by Power Grid Corporation of India Limited (PGCIL) to build sub-stations in India. The aforesaid contract comprised offshore supply, onshore supply, and onshore services covered under separate agreements.

As per the agreement pertaining to onshore services, TBEA China was to provide services encompassing inland transportation and civil work within India. Pursuant to the same, TBEA China set up a Project Office (PO / taxpayer) in India. This taxpayer constituted a Fixed Place Permanent Establishment (PE) of TBEA China in India as per Article 5(1) of the India-China Double Tax Avoidance Agreement (DTAA).

The HO was responsible for executing the offshore portion of the contract, whereas the taxpayer was responsible for the onshore portion. The taxpayer subcontracted a portion of the onshore work to independent third-party contractors in India. The HO received payments in relation to all the contracts, and it passed on the portion relating to the onshore work to the taxpayer subsequently, as the taxpayer did not have a bank account in India at the relevant time.

India's tax authorities adopted the stance that the act of the taxpayer carrying out the execution of the contract by providing services and thereby incurring expenses, which were subsequently passed on by the HO, was an international transaction between the HO and taxpayer.

Accordingly, the Transfer Pricing Officer (TPO) subjected the transaction under consideration to the arm's length standard and observed that the rate per unit of civil work received by the taxpayer from the HO (which in turn was received by the HO from PGCIL) was lower than the rate paid by the taxpayer to third-party sub-contractors. Hence, the TPO opined that the taxpayer was not adequately compensated for services rendered by it, resulting in losses.

The pertinent question before the SB was whether the transactions between a foreign enterprise and its Indian PE are international transactions within the purview of Section 92B of the Act and consequently, would be subject to ALP adjustment under transfer pricing regulations.

The ITAT SB observed:

- Under the Act as well as the Rules, the applicability of transfer pricing is dependent upon whether an entity qualifies as an "enterprise" or not as defined under Section 92F of the Act.
- "Enterprise" as per Section 92F of the Act is defined as " "enterprise" means a person (including a permanent establishment of such person) who is, or has been, or is proposed to be, engaged in any activity, relating to the production, storage, supply, distribution, acquisition or control of articles or goods, or know-how, patents, copyrights, trade-marks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights, or the provision of services of any kind, or in carrying out any work in pursuance of a contract, or in investment, or providing loan or in the business of

acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate, whether such activity or business is carried on, directly or through one or more of its units or divisions or subsidiaries, or whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or places."

- Given that the definition explicitly includes PE, the ITAT SB adjudicated that PE qualifies as an enterprise.
- The ITAT SB also observed that as per Article 7(2) of the India-China DTAA (which governs attribution of business profits), it is clear that a PE shall be attributed profits which it would be reasonably expected to earn in its capacity as a distinct and separate enterprise.
- It was further observed that Article 9 of the DTAA, dealing with AEs, is limited to only confirming that broadly similar rules exist in domestic law, and Article 9(1) by itself does not fulfil any necessary function as it only formulates rules that may already exist in domestic laws. Hence, even if the taxpayer's contention that provisions of DTAA override the Act was to be accepted, as per Article 7 of the DTAA profits need to be attributed to the PE.
- The SB specifically held that the taxpayer's contention that there are only fund movements between the HO and PO is not acceptable, as in an unrelated scenario an enterprise would not permit its receipts and payments to be routed through a third party.
- The revenue of the taxpayer is influenced by the agreement signed by the HO with PGCIL and hence, the taxable income in the hands of the taxpayer is dependent upon the HO.
- The definition of transaction under Section 92F(v) of the Act includes arrangement, understanding, or action in concert. Thus, the arrangement/ understanding between two enterprises giving rise to income or loss may be subject to transfer pricing.
- Given this, the transaction between the HO and the taxpayer would qualify as a transaction between two AEs which should be subject to ALP determination under transfer pricing regulations.

Citation: TBEA Shenyang Transformer Group Company Limited [TS-508-ITAT-2024(Ahd)-TP]

Hon'ble Tax Tribunal, Mumbai: Deletes TP-adjustment qua management fee payment; holds that whether the business decision was commercially sound or not is not relevant, the only question is whether the transaction, which was entered into, was bonafide or not, or whether it was a sham transaction only for the purpose of diverting profits.

Otis Elevator Company (India) Limited (taxpayer) is engaged in the business of manufacture, erection, installation, and maintenance of elevators, escalators, and other lifting and handling equipment. During the year under consideration, the taxpayer had entered into several international transactions with its Associated Enterprises (AEs).

In the course of assessment proceedings, the matter was referred by the Assessing Officer (AO) to the TPO. The TPO accepted all the international transactions to be at arm's length, except for the transaction pertaining to payment of management fees to Otis Asia-Pacific (APAC) headquarters, which had been allocated to the taxpayer on a cost plus 5% markup.

In response to the show cause notice (SCN) issued by the TPO, the taxpayer submitted various documentary evidence such as the rationale for availing services from the AE which houses qualified and experienced personnel, benchmarking analysis, and other relevant details.

However, the TPO opined that in the case of the taxpayer, commercial expediency of the international transaction relating to management services was not being examined, and instead, an exercise was being undertaken to check whether the taxpayer passed the need-benefit evidence test. Accordingly, the TPO concluded that the taxpayer had failed to furnish evidence in respect of the cost incurred by the AE for providing the said management services, and the transaction was effectively leading to profit shifting and base erosion, which was not permissible as per Indian transfer pricing regulations. The TPO made an upward adjustment considering the arm's length price (ALP) of management fees to be nil.

The taxpayer filed objections before the Dispute Resolution Panel (DRP), however, the TPO's order was upheld. Aggrieved, the taxpayer filed an appeal before the Income-tax Appellate Tribunal (Hon'ble Tax Tribunal).

On analysing the facts of the case, the Hon'ble Tax Tribunal held that:

- It is for the taxpayer to determine whose services it desires to avail. Business decisions are at times good and profitable, and at times bad and unprofitable. Business decisions, in fact, can result in losses, therefore, whether the decision was commercially sound or not is not relevant.
- The only question is whether the transaction entered into was bonafide or was a sham transaction which is entered only for the purpose of diverting profits.
- The Hon'ble Tax Tribunal drew reference and support from the decision of Hon'ble Punjab & Haryana High Court in the case of *Knorr Bremse India Pvt Ltd [2015] 63 taxmann.com 186 (Punjab & Haryana)*.
- The Hon'ble Tax Tribunal further stated the Hon'ble High Court of Delhi, in the case of *Cushman Wakefield (India) (P.) Ltd. (2014) 46 taxmann.com 317 (Delhi)*, held that the AO / TPO cannot question the quantum of the fee, but can check if services were actually rendered, and if they are genuine and real.

Accordingly, the Hon'ble Tax Tribunal directed the AO/TPO to delete the TP adjustment.

Citation: Otis Elevator Company (India) Limited [TS-507-ITAT-2024(Mum)-TP]

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