BHUTA SHAH & CO LLP

CHARTERED ACCOUNTANTS

BSC BEACON

Tax & Regulatory Insights

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Glossary

ABBREVIATION	FULL FORM
ACIT	Assistant Commissioner of Income Tax
AE	Associated Enterprise
AGR	Adjusted Gross Revenue
Act	Income-tax Act, 1961
AO	Assessing officer
AY	Assessment Year
CBDT	Central Board of Direct Taxes
CIT	Commissioner of Income-tax
CPC	Centralized Processing Center
CCPS	Cumulative Convertible Preference Shares
CCIT	Chief Commissioner of Income Tax
CIT(Appeals) / CIT(A)	Commissioner of Income-tax (Appeals)
CBDT	Central Board of Direct Taxes
DCF	Discounted Cash flow
DDT	Dividend Distribution Tax
DTAA	Double Taxation Avoidance Agreement
DCIT	Deputy Commissioner of Income Tax
HC	High Court
Hon	Hon’ble
FTS	Fees for technical services
FDI	Foreign Direct Investment
ITC	Input Tax Credit
ITBA	Income Tax Business Application
ITAT	Income Tax Appellate Tribunal
IFSC	International Financial Services Centre
MFN	Most Favored Nation
NAV	Net Asset Value
PE	Permanent Establishment
PY	Previous Year
PCIT	Principal Commissioner of Income Tax
PCCIT	Principal Chief Commissioner of Income Tax
SC	Supreme Court
TDS	Tax Deducted at Source
TPO	Transfer Pricing Officer

I. Direct Taxes

A. Corporate Taxes

1. Supreme Court[1]: Holds that variable license fees paid by telecommunication companies is capital expenditure and should be amortised over the life of the license.

Background

In the year 1999, the National Telecom Policy, 1999 (new policy) substituted the National Telecom Policy of 1994 (old policy). Some of the key features of the new policy were:

a) The telecom operator licensee is required to pay to the Department of Communication (DoT), a one-time entry fee and additionally, a licence fee on a percentage share of gross revenue (adjusted gross revenue – AGR).

b) The entry fee (one-time fee) chargeable was payable by the existing operator up to 31 July 1999, calculated up to the said date and adjusted upon notional extension of the effective date.

c) From 1 August 1999, licence fee (variable fee) was payable on a percentage of the AGR earned.

d) The period of licence was 20 years from the effective date of the existing licence agreement, i.e. from 1994.

As per section 35ABB, any expenditure being in the nature of capital expenditure for acquisition of right to operate telecommunication services - either before the commencement of the business or thereafter and for which payment has actually

[1] Bharti Hexacom Ltd vs CIT [Delhi] [2023] [TS-605-SC-2023]

been made to obtain a licence, there shall be allowed for each of the relevant previous years, a deduction equal to the appropriate fraction of the amount of such expenditure.

Judgement of the Hon'ble Supreme Court

The question before the Hon'ble Supreme Court was whether the variable annual licence fee paid by the assesse was revenue in nature and to be allowed deduction under section 37 of the Act or it was capital in nature and accordingly was required to be amortised under section 35ABB of the Act.

The Hon'ble Supreme Court concluded that the payment of entry fee as well as the variable fee was capital in nature and to be amortised in accordance with the provisions of section 35ABB of the Act.

The Hon'ble Supreme Court laid down important principles for determining whether the expenditure is revenue or capital in nature and held that:

a) To determine an expenditure is capital or revenue in nature, the ordinary course of business usually adopted in that concern and the object of incurring the expenditure should be taken into account. What is material is the nature of right sought to be secured through the payment. An expenditure cannot be treated as a revenue expenditure simply because the payment is structured in instalments.

b) The test to identify whether an expenditure structured in the form of instalments is in the nature of a capital expenditure or revenue expenditure, is to first consider whether the payment made (in lump-sum or in instalments) relates to the acquisition / expansion of a capital asset, or for working of an asset to produce profits. Further, if it is determined that the payment is towards acquisition / expansion of a capital asset, then it needs to be verified if the payment has simply been chopped up into smaller sums payable in instalments only for the sake of convenience.

c) Where a transaction consists of payments in two parts - lump-sum payment at the outset, followed by periodic payments - the nature of the two payments would be distinct only when the periodic payments have no nexus with the original obligation of the taxpayer. Payments post 31 July 1999 was a continuation of the payment pre 31 July 1999 albeit in an altered format which did not take away the essence of the payment. It was a mandatory payment traceable to the license agreement as modified post migration to the new policy. Consequence of non-payment would result in ouster of the licensee from the trade. Thus, the payment was intrinsic to the existence of the licence as well as trade itself.

2. ***Mumbai ITAT[2]:*** *Excess Cash shown in books of accounts than the cash found during the survey proceedings, such difference in cash cannot be treated as unexplained expenditure under section 69C.*

Background

During the course of survey proceedings in the premises of the petitioner actual cash of INR 11,800/- was found as against the cash in hand shown in books of accounts of INR 18,00,312/- Since the petitioner has failed to reconcile the difference and also not provided the details asked by the AO, the AO treated the difference amount of INR 17,88,512/- as unexplained expenditure under section 69C.

On Ld. CIT(A) upheld the decision of AO to treat the difference as unexplained expenditure, since no evidence was presented by the petitioner.

The petitioner preferred an appeal before the Hon'ble ITAT on the ground that whether merely on the basis of the shortfall between the actual cash found during the survey proceedings and the cash shown in the books of the accounts, addition under section 69C is warranted.

Decision of ITAT:

Placing reliance on the judgments of the Allahabad High Court and the Co-ordinate Bench of Mumbai Tribunal, it was held in the case of the petitioner that the provisions of section 69C will not attract and the shortfall in the cash cannot be considered as an unexplained expenditure. The Hon'ble Tribunal drew attention to the decision in the case of Allahabad High court, wherein it was held that where money is found to be in excess of the amount recorded in the books of accounts,

[2] Almech Enterprise vs. ACIT [I.T.A. No. 2110/Mum/2023]

that itself will not be suffice to make in addition under section 69 or 69A of the Act. At the most the authorities could have presumed that the assessee has spent the difference amount somewhere.

Further, reliance was also place in the case of M/s Sarang & Associates Vs. DCIT wherein the Mumbai Tribunal was of the opinion that the addition made under section 69C, due to the difference in cash in hands as per books and cash found during survey is not sustainable as the source of such expenditure could be the cash in hand available with the assessee as per the books of accounts.

3. **Mumbai ITAT[3]:** *Doctrine of Merger: An intimation issued under section 143(1) merges with the assessment order under section 143(3). Therefore, any adjustments made in the intimation would be valid only if the same adjustment is made in the assessment order.*

Background

The assesse is a stock exchange company and filed its Return of Income for AY 2021- 22 on 12/02/21 declaring total income of INR 2049,74,12,520/-. The assesses return was processed by CPC and intimation was issued under section 143(1) of the Act determining total income of INR 2084,98,11,580/-.

The assesse while computing the total income claimed a deduction of abandoned project expenses amounting to INR 35,23,99,063/-. However, the same was disclosed by the tax auditor in its tax audit reported as capital expenditure and hence, the same was disallowed by the CPC under section 37(1) of the Act in the intimation issued under section 143(1) of the Act.

Aggrieved with the intimation, assesse preferred to the CIT (A). CIT(A) dismissed the case in favour of the revenue.

Decision of ITAT:

As the case of assesse was scrutinized under section 143(2) and assessment order under section 143(3) of the Act was passed, doctrine of merger comes into picture and therefore the adjustment made by the CPC gets merged into the order passed under section 143(3) and only the order under section 143(3) survives. Thus if no addition is there in the assessment order, as was the case, the whole issue becomes academic.

[3] National Stock exchange of India Limited vs DCIT [TS-611-ITAT-2023]

4. *Chandigarh ITAT[4]: Holds that assessing officers are not authorized to pick and choose a particular method of valuation as the option is specifically given to the Assessee as per Rule 11UA(2) of the Income-tax Rules.*

Background

I.A. Hydro Energy Pvt. Ltd (the assesse) was incorporated on 23 March 2017 and prior to that business was carried out as a partnership firm. On conversion of the partnership firm to company, all partners became shareholders. Unsecured loan given by the erstwhile partners was converted into equity shares which were issued at a premium. The assesse had allotted 2.25 crore shares with face value of INR 10 at a premium of INR 90. No consideration was received towards the equity shares.

Section 56(2)(viib) of the Act provides for taxation in the hands of the company issuing shares if it receives any consideration in excess of fair market value (FMV) of shares. section 56(2)(viib) of the Act provides that the fair market value of unquoted shares shall be the value (1) as may be determined in accordance with such method as may be prescribed under Rule 11UA i.e. Discounted Cashflow (DCF) or Net Asset Value (NAV) method or (2) as may be substantiated by the company to the satisfaction of the assessing officer. Rule11UA prescribes valuation methodology for arriving at FMV of immovable property, jewellery, shares – both quoted and unquoted etc.

Assessment was completed after making an addition of approximately INR 202.5 crore under section 56(2)(viib) of the Act alleging that the assesse had issued equity

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[4] I.A Hydro Energy Pvt ltd vs. ACIT [TS-603-ITAT-2023][CHD]

shares at a premium which is in excess of the fair market value of the shares.

The department rejected the DCF method (as prescribed under Rule 11UA(2)(b)) and valued the shares by NAV method (as prescribed under Rule 11UA(2)(a)), merely on the grounds there is a huge difference in the projected figures and the actual results.

Decision of ITAT:

The Hon'ble ITAT observed that courts and tribunals have invariably held that the assessing officers are not authorized to pick and choose a particular method of valuation as the option is specifically given to the assesse as per Rule 11UA(2) of the Income-tax Rules.

The assessing officer has the power to verify the method of valuation adopted by the assessee but the same cannot be substituted by NAV method once the assessee has exercised option of DCF valuation method. In view of this, the Hon'ble ITAT deleted the addition of 202.5 crores. Reliance was placed on various decisions.

The Hon'ble ITAT also observed that there is no case of application of section 56(2)(viib) of the Act to the facts of the case where pre-existed unsecured loans of partners / shareholders were converted to equity shares at premium and the facts of the assessment order do not indicate any case of tax abuse involved in such share conversion.

B. International Tax

1. ***Supreme Court[5]:** Holds that a notification under section 90(1) is necessary and a mandatory condition to give effect to a DTAA or any protocol changing its terms or condition, which has the effect of altering existing provisions of law..*

Further, the Hon'ble Apex Court held that for a party to claim benefit of a "same treatment" clause, based on entry of DTAA between India and another country which is member of OECD, the relevant date is entering into treaty with India, and not a later date i.e. when after entering into DTAA with India such other country becomes OECD member.

Background:

The questions for the interpretation before the Hon'ble Supreme Court were:

a) Whether there is any right to invoke the MFN clause when the third country with which India has entered into a DTAA was not an OECD member yet at the time of entering into such DTAA.

b) Whether the MFN clause is to be given effect to automatically or if it is to only come into effect after a notification is issued.

Judgement of the Hon'ble Supreme Court:

a) A notification under section 90(1) is necessary and a mandatory condition for a court, authority, or tribunal to give effect to a DTAA, or any protocol changing its terms or conditions, which has the effect of altering the existing provisions of law.

b) The fact that a stipulation in a DTAA or a Protocol with one nation, requires same treatment in respect to a matter covered by its terms, subsequent to its being entered into when another nation (which is member of a multilateral organization such as OECD), is given better treatment, does not automatically lead to integration of such term extending the same benefit in regard to a matter covered in the DTAA of the first nation, which entered into DTAA with India. In such event, the terms of the earlier DTAA require to be amended through a separate notification under section 90.

[5] M/s. Nestle SA Vs. A.O [Delhi] [TS-616-SC-2023]

c) For a party to claim benefit of a "same treatment" clause, based on entry of DTAA between India and another state which is member of OECD, the relevant date is entering into treaty with India, and not a later date, when, after entering into DTAA with India, such country becomes an OECD member, in terms of India's practice. In other words, the third country has to be a member of OECD at the time of entering into DTAA and not when the MFN clause is applied.

Our Comments

This decision is expected to have significant impact on considerable number of tax payers who have previously relied on the interpretation that the application of MFN clause is not obligatory. Going forward, it would be important to exercise the due diligence in evaluating the transactions with countries having the MFN clause to ensure proper compliance and ascertain appropriate tax liabilities.

2. Hon'ble High Court of Telangana[6]: *Expounds on Section 201 limitation period involving NR payees; Disagrees with Delhi HC.*

Background:

The assessee has entered into a Trademark Assignment Agreement (TAA) with two foreign companies viz., USB Farchim SA, Switzerland ('USB Switzerland') and USB Biopharma SPRL, Belgium ('USB Belgium') for purchase of certain trademarks for identical territories including India. For AY 2016-17, the Assessee had paid an amount of INR 115,04,00,000 to USB Switzerland and an amount of INR 244,16,00,000 to USB Belgium for purchase of the said trademarks.

A survey under section 133A of the Act was conducted on 30 December 2015 wherein it was also verified whether tax has been deducted at source (TDS) on the payments made to USB Switzerland and USB Belgium. As the Assessee had not

[6] Dr. Reddys Laboratories Ltd. vs. Deputy Commissioner of Income-tax [TS – 583 – HC – 2023 TEL]

withheld taxes on the remittances made to the above payees, proceedings under section 201 of the Act were initiated against the Assessee by treating the Assessee as 'Assessee-in-default' and passed the order dated 14 December 2018

The assessee had filed writ petition before the Hon'ble High Court of Telangana on the question whether the period of limitation stipulated in section 201(3) of the Act would apply to the Assessee especially when the same uses the expression 'a person resident in India.'

Judgement of Hon'ble High Court:

The Hon'ble High Court upheld the validity of TDS proceedings initiated against the assessee on payments made to non-residents as the same were concluded within a reasonable time period i.e., 2 years 9 months from the end of relevant FY. On what should be the reasonable period, the Hon'ble High Court underscores that there cannot be straight jacket formula but opines, "...one thing is very clear, when the legislature has prescribed a period of seven years as the limitation for a resident Indian, it would not be justified to read a limitation of less than seven years in the case of a non-resident. The difficulty that would accrue to realisation of tax qua a non-resident would be much more than that of a person, who is a resident."

Disagreeing with Delhi HC view in Bharti Airtel, HC observes, "when legislature has consciously not prescribed any time limit for an order under section 201(1) in so far a non-resident is concerned; the reason being that if the deductee is a non-resident, it may not be administratively possible to recover the tax from the non-resident. Therefore, it would be wrong to read into section 201(3) of the Act a period of limitation insofar non-resident is concerned; doing so would amount to legislating by the Court which is not permissible."

Further, the Hon'ble High Court held that "limitation period of seven years prescribed for a resident Indian would be a useful guide to determine what would be a reasonable period in the case of a non-resident." Also, the Assessee itself requested Revenue to keep section 201 proceedings in abeyance in view of AAR application which categorically runs counter to its contention that proceedings were concluded beyond limitation. Thus, the Hon'ble High Court dismissed the writ petition without any observations on merits of the case and allows the Assessee to seek statutory remedy.

*3. **Mumbai ITAT[7]:** Absent evidence of cost-allocation & actual incurrence, upholds taxability of reimbursement as FTS.*

Background:

The Assessee is a company incorporated in USA and a tax resident of USA having its registered office at Pittsburg, Pennsylvania, USA. It does not have any branch office or employees in India. The control and management of assesses affairs are situated entirely in USA. Therefore, assessee is a non-resident of India for direct tax purposes. Accordingly, it claimed DTAA benefit between India and USA and filed tax residency certificate issued by the USA Tax Authorities. During the year, Assessee offered service income of INR 3,63,32,796 received from Heinz India Private Limited ("Heinz India" now known as Zydus Wellness Products Limited) and taken credit of TDS of INR 93,55,689.

Further, the assessee has submitted the breakup of total amount received of INR 8,81,94,650 from Heinz India as royalty for trademark of Rs. 96,715; support services income INR 3,62,36,081; and cost allocation [recovery of expenses] of INR 5,18,61,854. It was submitted by the assessee that the royalty and support services income are declared in its return of income as taxable income and the cost allocation recovery is claimed as non-taxable.

With regard to the cost allocation arrangement of INR 5.18 Crores claimed as non-chargeable to tax, it was submitted that the same is in the nature of reimbursement without any mark-up. The Assessee has submitted an agreement entered by the assessee and Heinz India dated 4 January 2016 and they brought to the notice of the assessing Officer Article 5 and specifically brought to the notice Article 5(2)(d) that the parties agreed the mark-up of 0% share applied to cost of performing support services under this agreement.

Further, it is submitted that the reimbursement of expenditure will also not attract

[7] Kraft Foods Group Brands LLC v. ACIT (International Taxation) [TS-577-ITAT-2023(Mum)]

Article 12(4) and submitted that the relevant receipt of reimbursement of expenditure will not fall under ancillary and subsidiary to the application or enjoyment of the right etc., and it does not come under the provisions of make available clause.

After considering the submissions of the assessee, assessing Officer rejected the same and observed that Assessee has not provided any documentary evidence regarding the claim of classification of income under support services and reimbursement towards cost allocation arrangement. The DRP upheld the view of the assessing Officer.

Decision of ITAT:

On appeal, the Hon'ble Mumbai Tribunal confirms additions for cost reimbursement as fees for technical services (FTS) in the hands of Assessee received from the affiliates for provision of various services. The Hon'ble Mumbai Tribunal observed that the assessee has failed to prove the actual reimbursements and claimed the cost on ad hoc basis without proper allocation as per support service agreement, and thus, held that "When there is no basis of allocation or actual cost incurred for affiliates, it shows that the claim of the assessee is gross and there is no document to support this claim". Further, Hon'ble ITAT observes that "the assessee has entered into a support services agreement to provide support services through the various cost centers but failed to submit any details or proper factors or allocations basis to classify the various support service charges provided/collected from the various affiliates, in particular Heinz India". Merely because the parties agreed that a mark-up of 0% shall be applied to cost of support services does not mean anything unless and until a proper supporting documents are submitted explaining how the costs are incurred on behalf of affiliates and how it is to be considered as reimbursement. There cannot be any presumption as to reimbursement. Also, the Hon'ble ITAT held that first the Assessee has to prove that the cost allocations are falling under the category of reimbursement and then only they can claim the same as exempt under income tax or under treaty which was not done in the instant case.

4. ***Mumbai ITAT[8]:*** *Allows Mauritian entity to carry forward of LTCL along with DTAA exemption for STCG.*

Background:

The assessee is a company incorporated in Mauritius as public company limited by shares. The assessee is a tax resident of Mauritius as per the provisions of India – Mauritius Double Tax Avoidance Agreement ('DTAA' or 'Tax Treaty'). It had invested in the Indian securities directly under the Foreign Direct Investment (FDI) route or indirectly through its subsidiaries.

In the return of income, the assessee carried forward the long-term capital loss on sale of shares amounting to INR 14,35,11,469 but has claimed the Short-Term Capital Gains on sale of shares amounting to INR 2,19,26,65,193 as exempt under Article 13 of the India-Mauritius Tax Treaty. Thus, the assessee had opted for the benefit of DTAA for STCG and at the same time the benefit under Income Tax Act, 1961 for LTCL. The Assessing Officer did not allow carry forward of LTCL.

In the application filed before the DRP, it was held that '...Article 13 of the India Mauritius DTAA cannot be selectively applied. Hence, the assessee is not entitled to carry forward the Long-Term Capital Losses for the year under consideration i.e., AY 2017-18 to the subsequent years and the decision of the AO is upheld.'

Decision of ITAT:

On appeal, the Hon'ble ITAT allowed the carry forward of long-term capital loss under section 74(1) of the Act to the Assessee along with the exemption of short-term capital gain under DTAA. The Hon'ble ITAT observes that under the head capital gains, STCG / STCL and LTCG / LTCL are distinct and separate streams of income and thus, "the provisions of section 90(2) will apply to each stream of income and not the head of income".

The Hon'ble Mumbai ITAT had relied on the ruling of the Bangalore ITAT in the case of IBM World Trade Corp which was upheld by Karnataka HC, wherein it was held that "in case of multiple sources of income an Assessee is entitled to adopt provisions of the Act for one source of Income while applying the provisions of DTAA for the other source"; Further, the Hon'ble Mumbai ITAT also relied on co-ordinate bench ruling in the case of Dimension Data which in turn relied on IBM and ITAT Special Bench rulings in Montgomery Emerging Markets wherein it observed that

[8] Indium IV (Mauritius) Holdings Limited v. DCIT (International transaction) [TS-591-ITAT-2023Mum]

"long term capital gains and short term capital gains are separate sources of income and merely because these are clubbed under the same head of income, their identity as separate sources does not get obliterated".

C. Transfer Pricing

*1. **Bombay High Court**[9]: Transfer Pricing Adjustment should be proportionate to the value of international transactions.*

On the question before the Hon'ble Bombay High Court whether the Mumbai Tribunal was correct in holding that the transfer pricing adjustment should be done on the proportionate value of international transaction, it was held that benchmarking should be done only on the associated enterprises' transactions and not for the entire turnover. It would be pertinent to note that on a similar ruling, a special leave petition filed by the revenue authorities has been admitted by the Hon'ble Supreme Court.

[9] Principal Commissioner of Income-Tax v. Spicer India Ltd. (No. 1) [2023] 458 ITR 40 (Bom)

II. Goods and Services Tax

1) **Clarification on issues pertaining to taxability of personal guarantee and corporate guarantee in GST.**

    a) Issues a circular clarifying that when no consideration is paid by the company to the director in any form, directly or indirectly, for providing personal guarantee to the bank/ financial institutes on their behalf, the open market value of the said transaction/ supply may be treated as zero and hence, no tax to be payable in respect of such supply of services.

    b) To insert sub-rule (2) in Rule 28 of CGST Rules, 2017, to provide for taxable value of supply of corporate guarantee provided between related parties as 1% of the amount of such guarantee offered, or the actual consideration, whichever is higher.

    c) To clarify through the circular that after the insertion of the said sub-rule, the value of such supply of services of corporate guarantee provided between related parties would be governed by the proposed sub-rule (2) of rule 28 of CGST Rules, 2017, irrespective of whether full ITC is available to the recipient of services or not.

2) **Amnesty Scheme for filing of appeals against demand orders in cases where appeal could not be filed within the allowable time period.**

    a) The Council has recommended providing an amnesty scheme through a special procedure under 148 of CGST Act, 2017. For taxable persons, who could not file an appeal under section 107 of the said Act, against the demand order under section 73 or 74 of CGST Act, 2017 passed on or before the 31st day of March, 2023, or whose appeal against the said order was rejected solely on the grounds that the said appeal was not filed within the time period specified in Section 107(1)

b) In all such cases, filing of appeal by the taxpayers will be allowed against such orders upto 31st January 2024, subject to the condition of payment of an amount of pre-deposit of 12.5% of the tax under dispute, out of which at least 20% (i.e. 2.5% of the tax under dispute) should be debited from Electronic Cash Ledger.

c) This will facilitate a large number of taxpayers, who could not file appeal in the past within the specified time period

3) Recommendation for automatic restoration of provisionally attached property.

The Council has recommended an amendment in sub-rule (2) of Rule 159 of CGST Rules, 2017 and FORM GST DRC-22 to provide that the order for provisional attachment in FORM GST DRC-22 shall not be valid after expiry of one year from the date of the said order. his will facilitate release of provisionally attached properties after expiry of period of one year, without need for separate specific written order from the Commissioner.

4) Clarification on export of service.

The Council has recommended to issue a circular to clarify the admissibility of export remittances received in Special INR Vostro account, as permitted by RBI, for the purpose of consideration of supply of services to qualify as export of services in terms of the provisions of sub-clause (iv) of clause (6) of section 2 of the IGST Act, 2017.

5) Allowing supplies to SEZ units/ developer for authorised operations for IGST refund route

The Council has recommended to amend Notification No. 1/2023-Integrated Tax dated 31.07.2023 w.e.f. 01.10.2023 so as to allow the suppliers to a Special Economic Zone developer or a Special Economic Zone unit for authorised operations to make supply of goods or services (except the commodities like pan masala, tobacco, gutkha, etc. mentioned in the Notification No. 1/2023-Integrated Tax dated 31.07.2023) to the Special Economic Zone developer or the Special Economic Zone unit for authorised operations on payment of integrated tax and claim the refund of tax so paid.

III. CBDT Circulars & Notification

1. CBDT[10] clarifies on disclosure of 'person making substantial contribution' in Form 10B & 10BB.

Audit report in the case of a fund or trust or institution or any university or other educational institution or any hospital or other medical institution, under clause (b) of the tenth proviso to clause (23C) of section 10, or sub-clause (ii) of clause (b) of sub-section (1) of section 12A of the Act, as the case may be, is required to be furnished in Form No. 10B / Form No.10BB.

The CBDT had vide notification no. 07/2023 dated 21.02.2023 had notified new forms of audit report for trust or educational institution mentioned above wherein various new reporting requirements were added.

Representation were made to CBDT regarding difficulties being faced in reporting details of persons having made substantial contribution to trust or institutions and its relatives and concerns.

The CBDT examined the matter and through Circular, has clarified the following:

a) the aforesaid details (that is, of person making substantial contribution) may be given with respect to those persons whose total contribution during the previous year exceeds fifty thousand rupees;

b) details of relatives of such person, as referred to in (a) above may be provided, if available;

c) details of concerns in which such person, as referred to in (a) Details of

[10] Circular No. 17/2023 dated 09.10.2023

individuals making substantial contributions to trusts or institutions.

Its needs to be noted that the relaxation is provided only with respect to reporting requirement and does not provide any relief for the purpose of computation of income of trust or the institutions.

2. CBDT[11] notifies Form 56F with effect from 29.07.2021.

Deduction under section 10AA is available to assesses who derived profits and gains from an undertaking engaged in the export of article or thing etc. from a unit in special economic zone.

In order to claim deduction under this section, section 10AA (8) read with section 10A (5) provides that the deduction under section 10AA shall be allowed if a report of an accountant in prescribed Form is furnished before the specified date. The CBDT vide Notification, has now notified rules 16D. As per this rule the report of the accountant has to be furnished in Form 56F. The rule is effective from 29.07.2021.

3. CBDT[12] extends due-date for filing newly notified Form 56F for AY 2023-24 to 31.12.2023.

On consideration of difficulties arising to the taxpayers and other stakeholders in timely filing of report of accountant required to be filed under clause (8) of section 10AA read with clause (5) of section 10A of the Income -tax Act, 1961 on account of notification of relevant Form 56F on 19.10.2023 and with a view to avoid genuine hardship to such cases, the Central Board of Direct Taxes, in exercise of its powers under] 19(2)(b) of the Income Tax Act, 1961 , hereby extends the due date of filing of report of the accountant as required to be filed under clause (8) of section 10AA read with clause (5) of section 10A of the Act, for Assessment Year 2023-24 from the specified date under section 44AB to 31st of December, 2023.

4. CBDT[13] notifies Form 15CD for IFSC units as quarterly statement of foreign remittances.

Under the Act, a person responsible for paying to non-resident any sum whether taxable or not has to furnish information relating to payment of such sum in a form and manner as prescribed.

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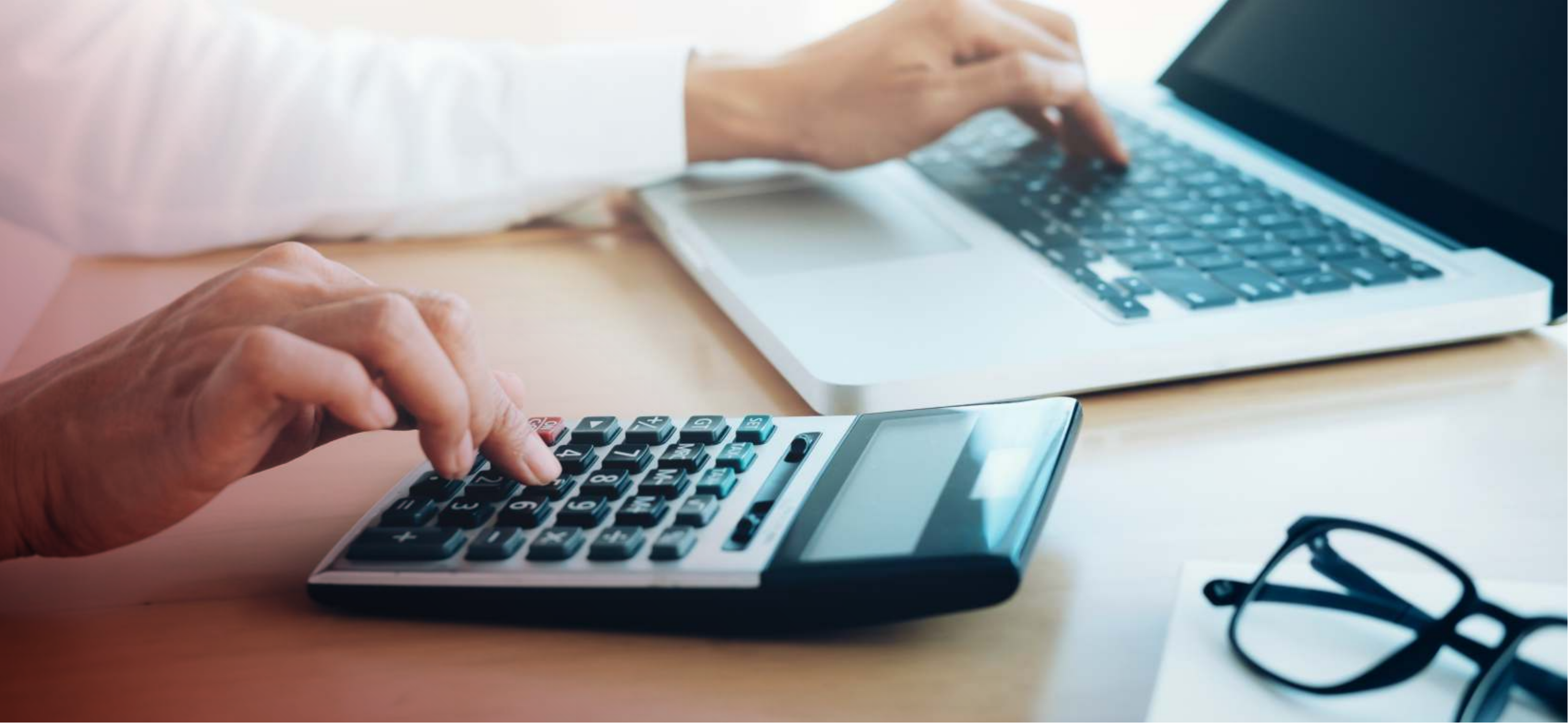
[11] Notification No. 91/2023/F. No. 370142/40/2023-TPL

[12] Circular No. 18/2023 dated 20.10.2023

[13] Notification No. 89/2023/F. No. 370142/36/2023-TPL



In pursuance thereof CBDT has introduced rule 37BB which prescribes the form and details to be furnished to the tax authorities.

The Central Board of Direct Taxes (CBDT) has introduced the Income-tax Amendment (Twenty-fifth Amendment), Rules, 2023 and amending Rule 37BB to exempt International Financial Services Centre (IFSC) Units from furnishing Part D of Form No. 15CA in respect of remittances not chargeable to tax in India.

In addition, rule 37BB has been amended to provide for furnishing quarterly statements in Form No. 15CD detailing all remittances made to non-residents or foreign companies by units in IFSC. This form must be furnished to the PDGIT/DGIT within 15 days from the end of the quarter to which such statement relates. The form seeks the following information:

a) Details of Remitter (Name, PAN/TAN, Residential Status and complete address)

b) Details of the Remittee (Name, PAN/Aadhar, complete address, country of residence)

c) Details of Remittance (Date, Amount and Nature of Remittance)

The provisions of this notification will be applicable from January 01, 2024.

3. CBDT[14] clarifies on recognised Start-up's assessments in light of Angel Tax amendment.

In this regard, the undersigned is directed to state that the Department for Promotion of Industry and Internal Trade (DPIIT) vide notification no. G.S.R. 127(E)

[14] F. No. 173/149/2019-ITA – dated 10.10.2023

dated 19.02.2019 provided for exemption for the purpose of clause (viib) of sub-section (2) of section 56 of the Income-tax Act, 1961 (the Act) for Startup company. By this notification, it has been provided that provisions of section 56 (2)(viib) of the Act shall not apply to Startup Companies which have been recognized by the DPIIT and fulfils the conditions mentioned in para 4(i) and 4(ii) of the said notification.

In pursuance to the above, the Central Board of Direct Taxes (CBDT) had issued notification no. 13/2019/F. No. 370142/ 5/2018-TPL(Pt.) dated 05.03.2019 notifying that the provisions of clause (viib) of sub-section (2) of section 56 of the Act shall not apply to consideration received by a company for issue of shares that exceeds the face value of such shares, if the said consideration has been received from a person, being a resident, by a company which fulfils the conditions specified in para 4 of the notification no. G.S.R.127(E) dated 19.02.2019 issued by DPIIT. The same was reiterated by CBDT Circular No.16/2019 dated 07.08.2019.

In this context, it is brought to notice that the Finance Act 2023 has amended clause

(viib) of sub-section (2) of section 56 of the Act and the words "being a resident" have been omitted w.e.f. 01.04.2024.

Instances of cases of Startups having been picked up for scrutiny under CASS have been reported. In the light of the above, the procedure as laid down with regard to the assessment of such Startup companies which have been recognized by the DPIIT and fulfilling the conditions mentioned in para 4(I) and 4(ii) of the DPIIT notification referred in para 2 above (hereinafter 'such Startup Companies') involving the issue of section 56(2)(viib) of the Act, is being re-iterated and it is clarified that;

a) Where the case of such Startup Company is selected under scrutiny on the single issue of applicability of section 56 (2) (viib) of the Act, no verification on such issues shall be done by the Assessing Officers during the proceedings under section 143 (2) or under section 147/143(2) of the Act and contention of such recognized Startup Companies on the issue will be summarily accepted.

b) Where the case of such Startup Company is selected under scrutiny with multiple issues including the issue u / s 56 (2) (viib) of the Act, the issue of applicability of section 56 (2)(viib) of the Act shall not be pursued during the assessment proceedings of such Startup Company. Due procedure be followed about other issues for which the case has been selected.

6. CBDT[15] condones Form 10-IC delay for AY 2021-22.

Representations was made to CBDT stating that Form No. 10-IC could not be filed for A.Y. 2021-22 within the due date or extended due date, as the case may be. It was requested that the delay in filing of Form No. 10-IC for A.Y. 2021-22 may be condoned.

On consideration of the matter, with a view to avoid genuine hardship to the domestic companies in exercising the option u/s 115BAA of the Act, CBDT in exercise of the powers conferred under section 119(2)(b) of the Act, has directed that the delay can be condoned for A.Y 2021-22 subject to condition mentioned below:

a) The return of income for relevant assessment year has been filed on or before the due date specified under section 139(1) of the Act;

b) The assessee company has opted for taxation u/s 11 SBAA of the Act in item (e) of "Filing Status" in "Part A-GEN" of the Form of Return of Income ITR-6; and

c) Form No. 10-IC is filed electronically On or before 31.01.2024 or 3 months from the end of the month in which this Circular is issued, whichever is later.

[15] Circular No. 19/2023 – dated 23.10.2023

IV. Audit and Assurance

1. MCA Notification on Dematerialisation of Shares as per Companies (Prospectus and Allotment of Securities) Rules, 2014

As per Rule 9 and 9A of Companies (Prospectus and Allotment of Securities) Rules, 2014, following sub rule shall be inserted after sub rule (1), namely:

1. As per sub rule (2), A public company which issued share warrants prior to the Companies Act and not converted into shares shall-
   a. within a period of **three** months must inform the registrar about the details of such share warrants in Form PAS-7; and
   b. within a period of six months requires the bearer of the shares to surrender such shares of the company to get it dematerialised in their account. The notice of such share warrant must be placed on the website of the company in Form PAS-8; if any and shall publish the same in a newspaper in the vernacular language which is in circulation in the district and in English language in an English newspaper widely circulated in the State in which the registered office of the company is situated.
2. As per sub rule (3), In case if the bearer of the shares does not surrender the share warrants as referred in sub-rule (2), the company shall convert it into dematerialised form and transfer it to IEPF under section 125 of the Act.
3. As per the newly inserted Rule 9B, every private company, other than a small company shall within the period referred to in sub rule (2) –
   a. Shall issue shares in dematerialised form and facilitate dematerialisation of

its all securities as per the provisions of the Depository Act, 1996 and its regulation made thereunder.

b. A Private company, which as on the last day of a financial year ending on or after 31st March 2023 is not a small company as per the audited financial statements for such financial year shall within eighteen months of closure of such financial year, comply with the provisions of this rule.

c. Every private company referred to in sub rule (2) making any offer for issue of any securities or buy back of securities or issue of bonus shares or right offer after the date when it is required to comply with this rule shall ensure that before making such offer entire of holding of securities of its promoter, director, Key managerial personnel have been dematerialized in accordance with the provisions of the Depository Act, 1996.

d. Every holder of securities of the private company referred to in sub rule (2) :

   i) who intend to transfer such securities on or after the date when the company is required to comply with this rule, shall get such securities dematerialized before the transfer or

   ii) who subscribed to any security of the concerned private company whether by way of private placement or bonus shares or right offer on or after the date when the company is required to comply with this rule shall ensure that all his securities are held in dematerialized form before such subscription.

4. The provisions of sub rule (4) to (10) of rule 9A shall, mutatis mutandis, apply to the demat3erialization of securities under this rule.

5. The provisions of this rule shall not apply in case of a Government company.

V. Navigating Liquidation Preference in Startup Fundraising

Introduction

In the startup world, where innovation and disruption flourish, securing successive rounds of funding is of utmost importance. Yet, beneath the surface, lie several unassuming concepts that can significantly impact the course of a startup's journey. In this article, we explore the essence of one such concept; Liquidation Preference, understanding its complexities, its influence on startup dynamics, and the delicate balance founders must strike to ensure an equitable outcome.

The Essence of Liquidation Preference

At its core, liquidation preference is a contractual clause that dictates the distribution waterfall for paying out the exit proceeds in the event of a company's liquidation, sale, or merger to its shareholders. It establishes a hierarchy, ensuring that certain shareholders, often referred to as preferred shareholders, recoup their investments before others participate in the distribution of proceeds. The liquidation preference sets a preference order for distribution of proceeds based on their share classes; Seed, Series A, B, C, etc. Based on the standard structure of liquidation preference, the lower down the Alphabet the shares are, the higher a seniority they hold. In the event of distribution of the proceeds, the entrants of the latest rounds receive their money first. While the clause seems like a reasonable safeguard for investors, it should be trodden carefully.

Liquidation Preference: A Double-edged sword

1. **Dilution Dilemma:** Liquidation preference, particularly in the form of

participating preferred shares, can dilute the equity and potential returns of founders and early-stage investors.

Picture a scenario where a startup raised ~$20 Mil in various fund raising rounds with $ 10 Mil coming from the late stage investor. Now, in case a liquidity event gets triggered in the Company and the best offer is to buy out the Company for say $ 12 Mil. In such a scenario, liquidation preference gets triggered and the late stage investor takes an accelerated exit. Out of the $ 12 Mil total consideration, the late stage investor takes $ 10 Mil to secure its capital, leaving behind only $ 2 Mil for all earlier investors and eventually nothing for the promoters. This can leave founders and the initial investors with a very small piece of the pie, despite their instrumental role in building the company.

2. **Impact on future funding rounds:** Offering Liquidation Preferences for prospective investors offers a sense of security and assurance, streamlining the fundraising process by instilling confidence and expediting negotiations. However, at the same time new investors may view the preferences granted to earlier investors as a threat to their own returns, potentially demanding more favorable terms, thereby leading to setting the bar of expectations for liquidation preference for each incoming investor. Therefore, it is necessary to draw careful terms right from the first round of investment.
3. **Excessive Burden on the Company:** The company may provide incoming investors with a liquidation preference as a multiple of their investment amount. However, in the event of the sale of the company, the exit corpus may not be enough to cover the total proceeds owed to the investors. This may lead to a scenario where all the shareholders need to mutually decide a haircut on the amount owed to them which can get challenging to achieve in a time-bound manner. Therefore, setting expectations which are not practical could make it difficult at times to settle and bring all parties to mutually agree upon the best possible outcome.
4. **Incentive Alignment:** In cases where existing investors hold significant liquidation preferences, the founders may not receive sufficient compensation, which can significantly impact their involvement and the alignment of incentives necessary for the company's growth. When prospective investors observe this situation, it may lead to a lack of enthusiasm for investing in a business where founders seem less committed to driving the company's growth.

Different types of Liquidation Preferences

While Liquidation Preference is a contractual agreement it is at the same time an art of negotiation, having multiple structures to capture multiple unpredictable scenarios, some of which are as under:

Based on returns (Capped Liquidation Preference):

a. Minimum Multiple of the Investment Amount (0.5x, 1x, 1.5x...)

b. Minimum IRR (i.e. 15%, 18%, etc)

Based on scenarios:

a. Good lever situation (founder's death, retirement,..)

b. Bad lever situation (fraud, default in material clauses of the agreement)

Based on Participation in Distribution of Proceeds:

a. Fully Participating Liquidation Preference

b. Non- Participating Liquidation Preference

Based on Seniority:

a. Standard Seniority

b. Pari Passu

c. Tiered

Navigating Liquidation Preference: A Founder's Dilemma

In the order to secure funding and steer clear of the downsides posed by liquidation preference, founders must exercise prudence and strategic acumen:

1. **Legal Counsel:** Founders should seek legal counsel to comprehensively understand the implications of liquidation preference and negotiate terms that protect their long-term interests. Legal experts can offer insights and strategies to ensure a fair and equitable arrangement.
2. **Balanced Negotiation:** Striking a balance between attracting investors and safeguarding their own interests is a delicate art. Founders must negotiate terms that foster investor confidence without jeopardizing their own stake in the company's success.

Conclusion:

VC liquidation preference clauses are a critical aspect of venture capital financing, offering benefits with equal part of exercising caution to founders, initial investors, and subsequent investors. While liquidation preference was not of significant importance during times of easy liquidity, it has taken center stage during challenging periods when startups face difficulties in raising subsequent rounds of funding. In these times, liquidation preference clauses have become most crucial, and those who had previously underestimated its importance, be they founders or investors, find themselves struggling to reach a common commercial ground.

Thus, it is crucial for all stakeholders to strike a balance between protecting their interests and fostering a positive, growth-oriented relationship to ensure the startup's success. Understanding the implications of liquidation preferences and navigating them carefully is vital for everyone involved in the venture capital ecosystem.

VI. Compliance Calendar Nov. 23

A. Income Tax

Sr No.	Due Dates	Concerned (reporting) Period	Compliance Detail	Applicable to
1.	7th Nov	October 2023	TDS / TCS Payment	Non-Government Deductors
2.	15th Nov	Form 16A (July to Sept.)	Salaried Employees	All deductors
3.	30th Nov	Financial Year 2022-23	Safe Harbour Form 3CEFA	Assesses covered under Transfer Pricing
4.	30th Nov	Financial Year 2022-23	Transfer pricing Master file Form 3CEAA	Assesses covered under Transfer Pricing
5.	30th Nov	Financial Year 2022-23	Transfer pricing CBCR Form 3CEAD	Assesses covered under Transfer Pricing
6.	30th Nov	Financial Year 2022-23	Filing of Income tax Return (Including partner of such firm covered under TP)	Assesses covered under Transfer Pricing

B. Goods and Service Tax

Sr No.	Due Dates	Concerned (reporting) Period	Compliance Detail	Applicable to
1.	10th Nov.	Oct. 23	GSTR – 7 (TDS)	Person required to deduct TDS under GST
2.	10th Nov.	Oct. 23	GSTR – 8 (TCS)	Person required to collect TCS under GST
3.	11th Nov.	Oct. 23	GSTR 1	a) Taxable persons having annual turnover > Rs. 5 crore in FY 2022-23 b) Taxable persons having annual turnover ≤ Rs. 5 crore in FY 2022-23 and not opted for Quarterly Return Monthly Payment (QRMP) Scheme

Sr No.	Due Dates	Concerned (reporting) Period	Compliance Detail	Applicable to
4.	13th Nov.	Oct. 23	GSTR – 1 (IFF)- QRMP	Aggregate Turnover is up to Rs. 5 crores
5.	13th Nov.	Oct. 23	GSTR – 6 (ISD)	Person registered as ISD
6.	20th Nov.	Oct. 23	GSTR – 3B	a) Taxable persons having annual turnover > Rs. 5 crore in FY 2022-23 b) Taxable persons having annual turnover ≤ Rs. 5 crore in FY 2022-23 and not opted for QRMP scheme
7.	13th Nov.	Oct. 23	GSTR - 5 (NRTP)	Non-resident taxable person (NRTP)
8.	20th Nov.	Oct. 23	GSTR - 5A (OIDAR)	OIDAR services provider
9.	25th Nov.	Oct. 23	GSTR – 3B - QRMP scheme- Monthly payment*	Aggregate Turnover is up to Rs. 5 crores

* D - Taxpayers who have availed the Quarterly Return Monthly Payment (QRMP), option having aggregate TO up to INR 50 Mn in PFY whose principal place of business is in Category -1 states

**E - Taxpayers who have availed the Quarterly Return Monthly Payment (QRMP), having aggregate TO up to INR 50 Mn in PFY whose principal place of business is in Category -2 states

C. FEMA Compliance

Sr No.	Due Dates	Particulars	Applicable to
1.	7th Nov.	ECB 2 Return (External Commercial Borrowing)	All Indian Borrowers who have non-resident lenders

D. Ministry of Corporate Affairs (MCA) Compliance

Sr No.	Due Dates	Particulars	Applicable to
1.	29th Nov.	Filing of Form MGT-7 Annual Return	For all Companies

BHUTA SHAH & CO LLP
CHARTERED ACCOUNTANTS

About us

Bhuta Shah & Co LLP (BSC) is a dynamic professional Chartered Accountants firm with a distinctive blend of skill sets, experience and expertise. Established in the year 1986, we operate from our Head Office in Nariman Point, Mumbai while having 6 offices across India in Mumbai, Pune, Ahmedabad and New Delhi.

We offer our clients a wide range of services including Audit & Assurance, Direct Taxation, Indirect Taxation, Transaction Advisory, Corporate Finance, Corporate Advisory, Risk Advisory, Cyber Security and Resolution & Insolvency Advisory.

We provide services to a diverse set of leading Indian and Multinational Clients, including FPIs, Mutual Funds, Large Banks, Broking Institutions, Listed Companies including Pharmaceutical Companies, Manufacturing Companies, Insurance Companies, Realty Companies, Jewellery Companies, Hospitals and several other Large and Medium Businesses.

Our forte is high quality services to our clients based on the core principles of Quality, Focus, Timeliness and Commitment.

The Leadership Team comes with rich experience and is supported by a competent and efficient team of Professionals including Chartered Accountants, Professionals with Big-4 Consulting and Industry experience, Advocates, Company Secretaries, MBAs, Former IRS Officers, who are committed to providing timely, professional and quality services to our clients.

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