

kcmInsight

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Dear Reader,

We are happy to present **kcmInsight**, comprising of important legislative changes in finance & market, direct & indirect tax laws, corporate & other regulatory laws, as well as recent important decisions on direct & indirect taxes.

We hope that we are able to provide you an insight on various updates and that you will find the same informative and useful.

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Detailed Analysis

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Understanding Quality of Earnings in Financial Due Diligence

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**Introduction**

In transaction due diligence and business valuation, normalisation of earnings is a crucial step to assess the accuracy, sustainability and reliability of a target's reported earnings. Earnings could be either gross profits, EBITDA, EBIT, profit before tax or profit after tax depending on the value driver in any deal. As part of financial due diligence, a comprehensive examination of the target's financial statements is made to help validate and negotiate an acceptable valuation which is most likely driven by the underlying earnings.

Normalisation of Earnings also known as "Quality of Earnings"

Quality of Earnings (QOE) is an in-depth analysis of a target's earning capacity from its core business activities. Unlike generalised financial metrics, which may include earnings derived from one-time or abnormal events, accounting adjustments, or non-operational activities, a QOE analysis focuses on validating the recurring, sustainable, operating and normalised income generated by the core business operations to provide a clearer view of the target's financial performance.

QOE analysis is generally performed during mergers and acquisition transactions, where buyers as well as sellers get to ensure that the transaction valuation is fair and reflective of the normal and sustainable business performance and accordingly plan for the post-acquisition integration. QOE analysis also assists in raising capital (debt or equity) from potential investors and lenders. QOE analysis is generally performed by external auditors or specialists involved in financial due diligence.

Key steps involved in review of Financial Statements**Revenue & Margin Analysis**

Provides insights into the drivers of revenue growth whether price driven, or volume driven, effectiveness of the sales strategy, market dynamics (demand and supply situation) of the products and/or services. Following key aspects are considered:

1. Review of revenue recognition policies being applied consistently to validate the timing and basis of revenue recognition.
2. Understand and validate key drivers of revenue being either price driven, or volume (scale) driven including change in

revenue mix by key products, services, customer segments, etc.

3. Evaluate gross margins over time for consistency and explain underlying variances / fluctuations.
4. Analyse if there is dependence on key customers and potential risk of loss of any major customer or end use market
5. Identify one-time revenues or revenues from operations to be discontinued

Expense Analysis

Helps break down each type of operational expense to understand where money is being spent and how it impacts business profitability. This information helps determine sustainable profitability and scalability of a business. Following aspects need to be kept in mind:

1. Review of the nature of costs (fixed vs variable) involved in the day-to-day operations of a business and how these costs correlate with the revenue generated including its growth.
2. Identify the non-recurring, extraordinary, or non-operating expenses that should be excluded for evaluation of the target business operations.

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- 3. Review the sustainability of the current operating expenses including workforce expenses, operating, selling and general overheads.
- 4. Understand related party transactions to ensure expenses are reported appropriately from an arms’ length perspective.

Asset and Liability Review

Evaluation of the target’s tangible and intangible assets, normalised operating working capital, any potentially overstated assets, undisclosed liabilities, or unrecorded items.

- 1. Understand the age of fixed assets and any discrepancy identified during physical verification of the assets
- 2. Analyse the ageing of receivables to understand any collectability issues or unusual terms with customers.
- 3. Review inventory turnover and valuation methods to identify any slow or non-moving or over-valued inventory.
- 4. Review completeness of liabilities, understand if payables are being stretched and normal payment terms with the suppliers, any contingent liabilities or off-balance sheet items.
- 5. Consider any unusual equity transactions or distribution to management in the form of dividends.
- 6. Evaluate the accuracy of prepaid expenses and accruals and if they are properly matched with the income statement.

Cash Flow Analysis

Provides vital information of how a business generates and spends cash and the target’s ability to sustain its operations, pay debts, and fund future

growth. Aspects to be considered include:

- 1. Compare operating cash flows with net income to check if earnings are supported by actual cash generation.
- 2. Review conversion of operating earnings to cash flows essentially to see if major portion of the earnings stays blocked in the working capital and is unrealised.
- 3. Review capital expenditures to see if these are sufficient to support envisaged growth as well as maintain normalised operations.
- 4. Assess the target’s ability to provide for debt service and interest service cover from the free cash flows available.

Normalization Adjustments

Based on review of the above-mentioned aspects, reported earnings are normalised to adjust any non-recurring, non-operating or irregular incomes and expenses to arrive at an accurate view of business profitability. Examples of some adjustments are as follows:

Adjustment	Action	Source
Reclassification of other income	Adjust the revenue for any item reported as other income below EBITDA but are operating in nature and vice versa	Disclosure in financial statements
One-off revenue and cost (above EBITDA)	Adjust if not related to the core business activity and unlikely to repeat or recur in future	Management disclosure, revenue and costs variance analysis

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Adjustment	Action	Source
Non-operating expenses	Where non-operating expenses are included in the target business financials, it must be adjusted	Management disclosure
Inventory related adjustment	Provide for provision of slow/non-moving inventory and improper valuation as suggested in the accounting standards	Accounting policies, inventory valuation and verification reports
Discontinued operations	Adjust revenue and costs related to products or services that will not continue post transaction	Disclosures made in notes to audited accounts
Cut-off adjustments	Review end-of-year provisions and accruals or incorrect timing or basis of revenue recognition	Audit adjustments, post-year-end events, accruals, provisions and cutoff considerations
Proforma revenue and costs	Adjust revenue and costs to be incurred to sustain operations or new avenues of revenue	New products, acquisitions, new markets

Adjustment	Action	Source
Transactions at non-market terms	Related party transactions above or below market rates, salaries and bonuses to management considered unreasonable	Related party transaction disclosures, transfer pricing reports

Conclusion

Normalisation of earnings is vital in determining transaction value in M&A transactions and providing an unobscured view of a target's profitability by focusing on sustainable, repeatable earnings to ensure that the multiples based valuation being paid in a transaction is fair. Negotiations and further discussions are done in relation to these normalisation adjustments while finalising the definitive agreements in a transaction. QOE analysis not only helps in validating financial performance but also strengthens stakeholder confidence by ensuring transparency in financial reporting post-acquisition.

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Important Rulings

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Receipt towards co-marketing agreement held as Capital Receipt

Satiofi Healthcare India Private Limited [Income Tax Tribunal Appeal No.138 of 2007 - Order dated 18 November 2024 (Telangana HC)]

The taxpayer, engaged in manufacturing and selling Hepatitis-B vaccines, entered into a co-marketing agreement with Pfizer Ltd., agreeing to produce vaccines in bulk for Pfizer, which would handle their promotion and sale. Revenue treated the payment received under the agreement as a revenue receipt, arguing that the taxpayer retained its trading rights, did not transfer any capital asset to Pfizer, and continued its business operations unaffected. Revenue contended that the agreement was part of the taxpayer's usual business activity, involving only the sale of vaccines, and did not impact its trading structure or income sources.

Conversely, the taxpayer argued that the amount received under the agreement represented compensation for transferring technical know-how and relinquishing rights to any new Hepatitis-B vaccine it might develop. The taxpayer claimed that the payment was a

capital receipt because it surrendered a capital asset in the form of technical know-how and entered into a non-compete agreement, which impaired its profit-making apparatus and adversely impacted its market share and brand.

The High Court ruled in favour of the taxpayer, emphasizing that agreements must be interpreted holistically, considering the parties' intentions. It concluded the payment was a capital receipt because:

- The taxpayer granted Pfizer rights to market and sell its patented product.
- Pfizer gained exclusive co-marketer rights and a right of first refusal for any new Hepatitis vaccine developed by the taxpayer.
- The taxpayer relinquished its right to grant marketing rights for new products to third parties.
- At the agreement's conclusion, Pfizer could manufacture or source similar products.
- The payment was not for purchasing stock but for relinquishing rights in patents and trademarks.

- The agreement imposed restrictive covenants and required the taxpayer to share technical and developmental information with Pfizer.

The Tribunal held that the payment received by the taxpayer under the co-marketing agreement was in exchange for surrendering rights in capital assets, including patents and trademarks. It emphasized that the agreement imposed restrictive covenants, limiting the taxpayer's ability to independently market or develop new products and impaired the taxpayer's profit-making apparatus. Therefore, the Tribunal concluded that the payment constituted a capital receipt.

This judgment highlights the importance of interpreting agreements holistically, focusing on their commercial intent and the impact on the taxpayer's trading structure. When a taxpayer enters into restrictive covenants that impair its profit-making apparatus, the resulting compensation should be classified as a capital receipt, even if integrated with business arrangements. Notably, the Tribunal in this case did not address the taxability of the capital

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receipt as income under the head of 'capital gains.' However, in such scenarios, since there is a relinquishment of rights in a capital asset (such as a patent or trademark), the transaction may be regarded as a capital gains transaction and, therefore, might still fall within the scope of taxability.

Taxpayer can claim benefit u/s 115BAB in subsequent year upon commencement of manufacturing

Granules CZRO Private Limited [ITA No.706/Hyd/2024 - Order dated 15 October 2024 (Hyderabad ITAT)]

The taxpayer was set up on 16 January 2023, and filed its return of income for the year ending 31 March 2023 along with Form 10ID before the due date of filing return. The taxpayer had availed benefit of section 115BAB of the ITA. However, the Revenue denied the claim u/s 115BAB, arguing that the taxpayer had not commenced production in AY 2023-24.

The Hyderabad ITAT noted that for availing benefit of section 115BAB of the ITA, the company should have been setup on or after 1 October 2019 and should have commenced

manufacturing on or before 31 March 2024. The taxpayer had commenced manufacturing before 31 March 2024 but not before 31 March 2023. The Tribunal further observed that it is essential to file Form 10ID on or before the due date of filing return for the first assessment year commencing on or after first day of April 2020 to avail the benefit. The Tribunal held that in the present case the first assessment year was AY 2023-24, however the conditions of section 115BAB could not be fulfilled since Form 10ID was filed prior to commencement of manufacturing activities. It opined that taxpayer could not be expected to file Form 10ID in the first year showing commencement of manufacturing activities when the section allows commencement of manufacturing activities till 31 March 2024 to be eligible for benefit of section 115BAB. It further observed that the taxpayer was prohibited to file Form 10ID in subsequent year when actual manufacturing had commenced.

The Tribunal accordingly held that if the taxpayer could prove commencement of manufacturing before 31 March 2024, that should be construed as sufficient compliance for providing benefit in subsequent assessment

years. Hence, the Tribunal held that taxpayer was not eligible for beneficial provisions of section 115BAB for AY 2023-24 but that should not affect subsequent year's claim when Form 10ID could not be filed by the taxpayer.

This decision highlighted the necessity of a balanced interpretation of procedural and substantive provisions under the ITA. Historically, there have been conflicts and interpretative challenges concerning sub-sections (2) and (7) of section 115BAB. The Hyderabad Tribunal has offered clarity on this matter, delivering much-needed relief through its jurisprudence. While the judgment is directly applicable to taxpayers within the same jurisdiction, it may also serve as persuasive support for other taxpayers facing similar issues.

ITAT holds notices under section 148 barred by limitation where issued beyond 30 June 2021

Pushpak Realities Pvt. Ltd. [ITA No.4812, 4814, 4816 / Mum / 2024 – Order dated 7 November 2024 (Mumbai ITAT)]

Notices were issued for various assessment years to the taxpayer as follows:

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Assessment Year	Time Limit For Issuance of Notice (Within Six Years)	Date of issuance of original notice u/s 148	Date of providing information pursuant to Ashish Agarwal case	Date of issuance of notice u/s 148 post Ashish Agarwal case
2013-14	31 March 2020	23 April 2021	28 May 2022	29 July 2022
2014-15	31 March 2021	23 April 2021 & 26 April 2021	28 May 2022	31 July 2022
2015-16	31 March 2022	23 April 2021 & 26 April 2021	28 May 2022	28 July 2022

The Hon'ble Mumbai Tribunal observed that in the case of *Rajeev Bansal*, the Revenue had conceded that for AY 2015-16, all notices issued on or after 1 April 2021, must be dropped, as they will not fall for completion during the period prescribed under TOLA. The Tribunal further discussed that the Hon'ble SC in *Rajeev Bansal's* case had noted that after 1 April 2021, the new regime had specified different authorities for granting sanctions u/s 151 of the ITA. This change, being more favourable to the taxpayer as it required approvals from higher authorities compared to the old regime, the SC held that in terms of Ashish Agarwal's judgement, any sanction granted after 1 April 2021, must comply with the provisions of section 151 under the new regime. The SC also held that the failure of the AO to adhere to the time limits prescribed u/s 151 affected the jurisdiction to issue a notice u/s 148 of the ITA.

The Tribunal highlighted that the SC clarified that the time limit for issuing notices, where any action or proceeding fell for completion between 21 March 2020, and 31 March 2021, had been extended to 30 June 2021. Similarly, the time limit for granting sanctions was also extended to 30 June 2021. Consequently, for AY 2015-16, since the Revenue had already agreed that the notices must be dropped, the Tribunal held that the notices were barred by limitation. For AYs 2013-14 and 2014-15,

the Tribunal ruled that the time limit for issuing notices had expired on 30 June 2021. However, since the notices u/s 148 were issued in July 2022, they were also deemed time barred.

The Tribunal's comparison of notices issued post-*Ashish Agarwal* judgement with the extended time limits under TOLA appears to misinterpret the concept of "time limit surviving under the Income Tax Act read with TOLA". The Tribunal while deciding for AY 2013-14 and AY 2014-15 concluded that notices under the amended provisions should have been issued by 30 June 2021. However, the Hon'ble SC in *Rajeev Bansal* clarified that the period between the original notice and the time taken by the AO to provide requisite information (along with two weeks granted to the taxpayer to respond) would be deemed to have been stayed.

An important aspect deliberated by the Tribunal was the requirement to obtain approval from the specified authority. For any reassessment approval granted after 31 March 2021, the approval must have been obtained from the authority specified under the amended provisions. While the Tribunal did not provide details on the dates of approval for the original

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notices, if such approval were not obtained in accordance with the amended provisions, this could serve as a valid ground for contesting the notices. The SC in *Rajeev Bansal* merely extended the time limit for obtaining approval by the specified authority to 30 June 2021. It did not, however, amend the provisions to allow the specified authority under erstwhile provisions to grant approval where approval has been obtained post 31 March 2021. Hence, any non-compliance with this requirement could render the notices invalid.

TDS u/s 194C not required on capital grant subsidy

National Highway Authority of India [ITA 1145/2017 & 159/2021– Order dated 12 November 2024 (Delhi HC)]

The taxpayer, National Highway Authority of India (NHAI), is a statutory body established under the National Highways Authority of India Act, 1988, responsible for the development, maintenance, and operation of National Highways. NHAI provided a capital grant subsidy to a Concessionaire under a Build-Own-Operate-Transfer (BOOT) model project. The Concessionaires develop roads and highways

based on the Public Private Partnership model. Revenue contended that NHAI failed to deduct TDS u/s 194C of the ITA on the subsidy. NHAI argued that the subsidy was financial assistance to ensure project viability and did not constitute payment for "work" u/s 194C.

Under the Concession Agreement, the Concessionaire was tasked with constructing, maintaining, and operating highways at its own cost and risk and was conferred with the right to charge and collect user fees during the concession period. Upon conclusion of this period, the highway would revert to NHAI. The capital grant subsidy was provided to address viability gaps in cases where revenue generation by concessionaire would be unable to cover the project cost. It was disbursed through a competitive bidding process and deposited into an Escrow Account. These funds were not discretionary payments to the Concessionaire but were strictly regulated for specified purposes during the concession period, as outlined in the agreement.

Revenue asserted that section 194C broadly covers payments for any "work" by a contractor and the word 'work' as it appears in section 194C should be conferred an expansive

meaning and thus not be restricted to a works contract alone. However, NHAI argued that the subsidy was neither payment for physical work nor remuneration for services performed but was financial support to bridge the viability gap.

The High Court, while analysing section 194C, observed that the term "work" primarily refers to activities involving labour or undertaking of a physical or tangible activity as opposed to the mere grant of subsidy or financial assistance. The Court emphasized that the BOOT model envisions the Concessionaire as the owner of assets during the concession period, bearing the financial responsibility for project creation and recovering costs through user fees. It concurred with the Tribunal's finding that viability gap funding served as financial aid for public utility creation. The Court concluded that the subsidy provided by NHAI as viability gap funding was not a payment for work u/s 194C. While section 194C is not limited to works contracts, the viability gap funding did not constitute recompense for any physical activity or labour, and thus, withholding tax provisions were inapplicable.

The Court's decision highlights the distinction between financial assistance, such as viability

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gap funding, and payments made for physical work u/s 194C. This decision ensures that subsidies designed to support public infrastructure development are not misinterpreted as taxable payments for work performed.

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Section 194N not to apply to Foreign Representations

Notification No. 123/2024/F. No. 275/39/2021-IT(B) dated 28 November 2024

Section 194N provides that institutions such as banks, co-operative societies engaged in banking business and post offices must deduct 2% tax on cash withdrawals exceeding INR 1 crore in a financial year from accounts maintained by the recipient. The Central Government after consultation with the RBI has specified that the provisions of section 194N shall not apply to Foreign Representations duly approved by the Ministry of External Affairs of the Government of India including Diplomatic Missions, agencies of the United Nations, International Organisations, Consulates and

Offices of Honorary Consuls which are exempt from paying taxes in India as per the Diplomatic Relations (Vienna Convention) Act 1972 (43 of 1972) and the United Nations (Privileges and Immunities) Act 1947 (46 of 1947). The notification shall come into effect from 1 December 2024.

CBDT sets monetary limit for interest waiver or reduction u/s 220

F.No.400/08/2024-IT(B) / Circular No. 15/ 2024 dated 4 November 2024

As per section 220(2) of the ITA, if a taxpayer fails to pay the amount specified in any notice of demand u/s 156 of the ITA, he / she shall be liable to pay simple interest at rate of 1% per month or part of the month for the period of delay in making the payment. Further, section 220(2A) of the ITA empowers the Principal Chief Commissioner (Pr.CCIT) or Chief Commissioner (CCIT) or Principal Commissioner (Pr.CIT) or Commissioner (CIT) for reduction or waiver of interest amount subject to fulfilment of the following conditions:

- (i) Payment of such amount has caused or would cause genuine hardship to the Assessee,

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- (ii) Default in payment was due to circumstances beyond the control of the Assessee, and
- (iii) Co-operation by taxpayer in inquiries related to assessments or recovery proceedings

CBDT vide circular dated 4 November 2024 in respect of interest waiver or reduction has specified monetary limits are as follows:

- Pr. CIT / CIT – Up to INR 50 Lakhs
- CCIT / DGIT - Above INR 50 Lakhs up to INR 1.5 Crores
- Pr. CCIT - Above INR 1.5 Crores

The waiver shall be subject to conditions of section 220(2A) of the ITA. The Circular has been made effective from 4 November 2024.

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Taxpayer eligible to choose beneficial provisions of Act or DTAA for different income streams

Morgan Stanley Mauritius Company Ltd [ITA No. 3316/MUM/2023 - Order dated 28 October 2024 (Mumbai ITAT)]

The taxpayer, a Mauritius tax resident registered as an FPI under SEBI's FPI regulations, engaged in portfolio investments in Indian securities. The taxpayer claimed an exemption on long-term capital gains from shares acquired before April 1, 2017, under the India-Mauritius DTAA. Additionally, the taxpayer carried forward unutilized short-term capital losses from prior assessment years.

The Revenue contended that the taxpayer should not selectively apply the DTAA to exempt long-term capital gains while utilizing domestic provisions to carry forward short-term capital losses. It argued that losses from exempt income sources should not enter the return of income, and capital losses exempted under treaty provisions cannot be carried forward for offsetting against future capital gains. The Revenue further asserted that taxable income

should be determined under domestic provisions, including carry-forward and set-off rules, before applying DTAA benefits, requiring prior losses to offset current gains.

The Tribunal ruled in favour of the taxpayer, holding that income streams must be treated distinctly, allowing separate applications of beneficial provisions from the DTAA and the ITA for long-term capital gains and carried-forward short-term capital losses. It emphasized that taxpayers could independently invoke treaty benefits under Article 13 for long-term capital gains while continuing to carry forward losses under the ITA for prior years. The decision reaffirmed that taxpayers can selectively apply DTAA benefits without needing uniform adoption across the same income category.

No tax liability in absence of PE on sale of software licenses

Tricentis GmbH [ITA No. 2705 & 3526 /Del/2023 - Order dated 7 November 2024 (Delhi ITAT)]

The taxpayer, an Austrian tax resident, was engaged in the business of providing software quality assurance solutions by selling licenses for its testing software. It earned income from Indian customers through the sale of end-user

licenses and provision of support and consultancy services. Historically, the taxpayer had offered income from software license sales as royalty for taxation purposes. However, for the year under consideration, it claimed exemption based on the Supreme Court's ruling in Engineering Analysis Centre of Excellence Pvt Ltd.

The Revenue observed that most patents owned by the taxpayer were registered in jurisdictions other than Austria. It argued that the determination of "economic ownership" of intellectual property (IP) depends on the development, enhancement, maintenance, protection, and exploitation (DEMPE) functions. Applying the principle of "substance over form," the Revenue asserted that although the taxpayer was the legal owner of the IP, it lacked the economic substance to substantiate IP ownership in Austria. Citing the BEPS Action Plans 8-10, the Revenue contended that the economic ownership primarily resided in the U.S. and alleged that the contractual transfer of software to the taxpayer was structured to facilitate tax avoidance in India, the U.S., and Austria. It further alleged treaty shopping, suggesting the Austrian entity was incorporated

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to exploit favourable tax treaties and avoid U.S. worldwide taxation. As the taxpayer lacked commercial rationale for its Austrian incorporation under the cost-sharing arrangement, the Revenue treated income from software sales as business income taxable in India.

The taxpayer countered that it had been incorporated in Austria since 2007, continuously engaged in developing and selling testing software. It presented a valid Tax Residency Certificate (TRC) and referenced judicial precedents asserting that a TRC is sufficient to establish treaty eligibility unless fraud or illegality is proven. The taxpayer highlighted that it had employed adequate number of employees and had incurred expenditure on research and development. It argued that IP registration in other jurisdictions did not negate its ownership. Additionally, the sales in India were conducted on a principal-to-principal basis, with no transactions occurring within India, rendering section 9(1)(i) of the ITA inapplicable.

The Tribunal noted that the taxpayer's ultimate parent company was U.S.-based but emphasized the primacy of the TRC in determining tax

residency absent any fraudulent activity. It held that the Revenue bore the burden of proving fraud or illegality to deny treaty benefits. The taxpayer had demonstrated substantial operations, including filing tax returns, and being assessed by Austrian authorities. Furthermore, Indian sales constituted only a minor portion of the taxpayer's global revenues. The Tribunal found the Revenue's treaty shopping allegations speculative, unsupported by concrete evidence, and outside the jurisdiction of Indian tax authorities, as any concerns regarding U.S. tax avoidance fell under the purview of U.S. authorities.

The Tribunal also clarified that the BEPS Action Plan lacks direct applicability in judicial determinations in the absence of corroborative evidence. It concluded that IP ownership remains with the taxpayer regardless of IP registration in other jurisdictions. As the software license income was characterized as business income and no PE was established in India, the income could not be taxed in India under the India-Austria DTAA.

The Tribunal in this case has reiterated the importance of TRC and held that onus of proving

fraudulent intention or treaty shopping lies on the revenue where taxpayer holds a valid TRC.

Code sharing arrangements eligible for benefit of Article 8 of India-US DTAA

Delta Air Lines Inc [ITA No. 235/Mum/2022 - Order dated 7 November 2024 (Mumbai ITAT)]

The taxpayer, a U.S.-based airline operating in international traffic, established a branch office in India to manage air passenger ticket and freight bookings which constituted a PE in India. The taxpayer earned revenue, including income from code-sharing arrangements. In such arrangements, the taxpayer (the marketing airline) sold tickets for flights operated by third-party carriers (the operating airline), enabling the taxpayer to serve destinations or segments it did not operate directly.

The AO contended that income from code-sharing arrangements did not qualify as profits derived from aircraft operations under Article 8(1) of the India-U.S. DTAA. The AO argued that such income was unrelated to the taxpayer's direct operation of aircraft, as the actual transportation was carried out by third parties. Applying Rule 10 of the Income Tax Rules, the AO computed taxable income by adjusting the

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taxpayer's Global Profitability Rate (GPR) to account for code-sharing revenue.

The Tribunal interpreted that the term "operation of aircraft" under Article 8(1) encompasses chartering arrangements, including partial charters, such as booking space on third-party aircraft. Drawing parallels with slot-chartering arrangements in shipping, it clarified that an airline could be considered a "charterer" even if it only books specific space or seats on a third-party flight. It emphasized that under code-sharing arrangements, passengers are transported through third party airlines and tickets for the entire journey are issued by the taxpayer bearing its unique code. This arrangement, it noted, directly links the revenue earned to the taxpayer's core business of aircraft operation. Such activities, the Tribunal noted, allowed the taxpayer to expand its services and customer base without additional operational resources.

The Tribunal rejected the Revenue's argument that the absence of specific seat allocations disqualified the arrangement as chartering. Instead, it found that code-sharing agreements effectively block seats on third-party airlines for the taxpayer's passengers, meeting the

requirements for operations of aircraft in international traffic under Article 8(1) of DTAA. Referring to the OECD Model Commentary, the Tribunal held that code-sharing agreement is inherently connected to international traffic and qualifies as profits from aircraft operations under the treaty.

In distinguishing this case from an earlier ruling delivered in case of the taxpayer by a co-ordinate bench, the Tribunal highlighted subsequent judicial developments and unconsidered technical aspects. In conclusion, the Tribunal ruled that income from code-sharing arrangements qualifies for exemption under Article 8(1) of the India-U.S. DTAA, recognizing it as profits from international aircraft operations.

Tribunal underscored the importance of not blindly following prior decisions, especially when material facts or legal interpretations have evolved.

Arbitration award is business income - not taxable in absence of PE

Fujitsu Ltd [ITA No. 2607/Del/2022 - Order dated 14 November 2024 (Delhi ITAT)]

The taxpayer, a tax resident of Japan, was engaged in providing IT support, maintenance, and software licensing services. During the year under consideration, the taxpayer received proceeds from an arbitral award against Mahanagar Telecom Nigam Limited (MTNL), including interest accrued on fixed deposits on amount which was deposited during the pendency of execution proceedings. The taxpayer contended that the arbitral award arose from a contractual obligation and constituted business income, not taxable in India due to the absence of a PE in India. The taxpayer argued that the AO had misinterpreted the arbitral award and its clauses, asserting that it was a party to the award and had privity of contract with MTNL as a member of the consortium which was awarded the contract by MTNL. The taxpayer contended that the compensation was directly linked to the supply of equipment and thus bore the character of business income.

The AO, however, classified the compensation as a one-time, unforeseeable windfall gain rather than business income. The AO reasoned that the taxpayer lacked a direct contractual relationship with MTNL, played only a subsidiary

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role in the consortium, and did not incur any business expenses in India. As a result, the AO characterized the compensation as "income from other sources" under the ITA and deemed it taxable under Article 22 of the India-Japan DTAA.

The Tribunal overturned the AO's findings, holding that the compensation received through the arbitral award was for unpaid dues related to offshore supplies made by the taxpayer. It concluded that the compensation clearly constituted business income, arising from the taxpayer's contractual obligations. Under Article 7 of the India-Japan DTAA, such business income was not taxable in India in the absence of a PE. Further, relying on the Supreme Court judgment in *Govinda Choudhary & Sons (203 ITR 881)*, the Tribunal held that interest on compensation from the arbitral award also retained the character of business income rather than "income from other sources."

The Tribunal emphasized the principle that income derived in connection with business activities takes its character from the principal business activity, even if such receipts are one-time in nature. It emphasized that the classification of income should be based on the nature of the underlying activity, asserting that

compensation linked to a business activity inherently derives its nature and treatment from that activity.

Foreign Rulings**German Tax Court allows refund of withholding tax to non-resident investment funds**

[ECLI:DE:BFH:2024:U.130324.IR2.20.0 - Order dated 13 March 2024 (German Federal Fiscal Court)]

Taxpayer, a foreign investment fund had received dividend from domestic stock corporation subject to tax withholding in Germany. The Federal Fiscal Court ruled on whether a foreign investment fund, a Luxembourg-based Société d'Investissement à Capital Variable (SICAV), was entitled to a refund of German tax withheld on domestic dividends. The Court found that the exclusion of foreign funds from tax exemptions granted to domestic funds under the 2004 Investment Tax Act violated the free movement of capital under EU law. Consequently, the foreign fund was entitled to a refund of the withheld tax, as the discrimination against foreign funds could not be justified under EU law.

The Court emphasized that Section 11 of the Investment Tax Act, which restricts tax exemptions to domestic funds, breached EU principles by deterring cross-border investments. It relied on the European Court of Justice's judgment in a similar case (C-537/20) to affirm that foreign funds in comparable situations must receive the same tax treatment as domestic funds. The discriminatory treatment was neither necessary nor proportional to maintaining coherence in the tax system.

Additionally, the Court ruled that the foreign fund was entitled to interest on the refunded tax. It clarified that Member States are obligated under EU law to compensate taxpayers for the unavailability of funds due to taxes levied unlawfully.

The case was referred back for further proceedings and the lower court was tasked with verifying the accuracy of the refund amounts and calculating the interest due to the fund. The Federal Fiscal Court also addressed procedural matters related to jurisdiction and reaffirmed its commitment to upholding EU principles in tax cases.

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Foreign Updates

Significant Economic Presence Tax to be introduced in Kenya

Tax Laws (Amendment) Bill 2024 and the Tax Procedures (Amendment) (No.2) Bill 2024 has been placed in Kenya's National Assembly. The bill proposes to introduce Significant Economic Presence Tax (SEPT). This tax shall be payable by a non-resident person whose income from provision of services is derived from or accrues in Kenya through a business carried out over the digital marketplace. The proposed amendment is intended to replace Digital Service Tax with Significant Economic Presence.

Persons who shall be exempt from the SEPT are:

- (a) non-resident persons who offer digital services through permanent establishments in Kenya
- (b) non-resident persons who carry on the business of transmitting messages by cables, radio, optical fibre, television, broadcasting, internet, satellite, or other similar methods of communication

(c) non-resident persons providing digital services to an airline in which the government of Kenya has at least forty-five per cent (45%) shareholding.

For the purposes of computing the SEPT, the taxable profit of a person liable to pay the tax shall be deemed to be ten per cent of the gross turnover. The rate of tax in respect of SEPT charged shall be thirty per cent of the deemed taxable profit.

A person subject to SEPT shall submit a return and pay the tax due to the Commissioner on or before the twentieth day of the month following the end of the month in which the service was offered.

France introduces New Temporary Contribution on Corporate Income Tax of large companies

On 10 October 2024, the Government of France presented the draft Finance Bill for 2025. The Bill is expected to be finalised and enacted by the end of December.

Companies with annual turnover in France of at least EUR 1 billion would be subject to an exceptional surtax on corporate income tax. This

surcharge would apply to the two consecutive fiscal years ending on or after 31 December 2024, and would be based on the corporate income tax and assessed before offsetting any tax reductions, tax credits or tax receivables.

The rate of the exceptional contribution would depend on the turnover generated and the financial year concerned. For the first FY ending on or after 31 December 2024, the rate of the surtax would be equal to:

- 20.6% for standalone companies or tax-consolidated groups with revenue realized in France equal to or greater than EUR 1 billion, but less than EUR 3 billion.
- 41.2% for standalone companies or tax-consolidated groups with revenue realized in France equal to or greater than EUR 3 billion

For the second FY ending on or after 31 December 2024, the applicable rates would be 10.3% and 20.6%, respectively.

The draft Finance Bill also provides for a mechanism to mitigate the threshold effects for

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companies with turnover between EUR 1 billion and EUR 1.1 billion or between EUR 3 billion and EUR 3.1 billion.

Taxpayers would be required to remit the contribution, which would not be tax deductible for corporate income tax purposes, no later than the corporate income tax balance payment date.

Estonian Parliament Approves EU Small Business Scheme for Cross-Border Supplies

On 13 November 2024, the Estonian parliament approved the Act amending the Value Added Tax Act and the Taxation Act (462 SE). The legislation primarily introduces the EU small business scheme for cross-border transactions, aligning with Council Directive (EU) 2020/285 of 18 February 2020. Under the new measures, taxable persons based in other EU Member States may qualify for a VAT registration exemption in Estonia if their annual turnover within Estonia does not exceed EUR 40,000 and their total annual turnover within the EU does not exceed EUR 100,000. Similarly, small businesses established in Estonia can apply for the exemption in other EU Member States, provided their annual EU-wide turnover does

not exceed EUR 100,000 and their turnover in the respective Member State stays below the applicable threshold. The amendment is set to take effect on 1 January 2025.

Turkey Reduces Capital Gains Tax Exemption on Shares

Turkey's Revenue Administration has announced the issuance of Presidential Decision No. 9160, published in the Official Gazette on 27 November 2024. The decision reduces the tax exemption on capital gains from the sale of participation shares held for a minimum of two full years from 75% to 50%. The revised exemption rate also applies to gains derived from founders' shares, redeemed shares, and pre-emptive rights held for the same duration. The change came into effect on 27 November 2024.

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**Advertisement and marketing expenditure controversy: Beginning of the end**

Whirlpool of India Ltd [SLP to Appeal (C) Nos. 29270 & 32338 of 2016 – Order dated 20 November 2024 (Supreme Court)]

In the Transfer Pricing space, the Special Leave Petition filed by the Indian income tax department assailing the order of the Hon'ble Delhi High Court in case of Whirlpool of India Ltd has been rejected by the Apex Court. The details forming part of the detailed judgment of the Delhi High Court are discussed in ensuing paragraphs.

The taxpayer was engaged in the production, sales, and distribution of consumer appliances marked under Whirlpool. The taxpayer had entered into various international transactions such as sale of finished goods, spares, purchase of spares, raw materials and various other transactions. While considering the above transactions, the TPO made special reference to the quantum of the advertisement, marketing and promotion ('AMP') expenses which was regarded as extremely high (ratio of the AMP expenditure to sales) when compared to the companies operating in similar businesses.

The TPO was of the view that the taxpayer by virtue of the excess AMP expenditure (as compared to the comparable entities) was creating "marketing intangibles" for the whole group and as a result, the whole group including the associated enterprise were enjoying the recall value of the brand which was emanating from such excess AMP expenditure. The tax department contended that the increased sales due to the aggressive marketing expenditure led to the promotion of the Whirlpool brand and as a result, the benefit arising out of the aforesaid expenditure will inure to the AE. The TPO made an adjustment for the recovery of the excess marketing expenditure so incurred and further applied a markup over and above the AMP expenditure as TPO was of the view that it constituted support services towards brand building exercise.

Aggrieved by the TPO's order, the taxpayer appealed before the CIT(A) and consequently, the Tribunal which upheld the actions of the TPO. Aggrieved by the aforesaid adjudicating authorities, the taxpayer made an appeal before the Hon'ble Delhi HC.

The Delhi HC approached the very nexus of the Indian transfer pricing regulations i.e., there should be an international transaction in actual existence to determine the ALP. In this regard, the Delhi HC, as a first measure, placed its reliance on its own ruling in case of Sony Ericsson wherein it was specifically held that the application of the Bright Line Test cannot be adopted for the existence and consequent determination of the ALP of an international transaction involving AMP expenditure. The Delhi HC specifically stressed upon the definition of transaction which includes an arrangement, understanding or action in concert i.e., two or more persons joining together with the shared objective. The element of the shared common objective or purpose is the sine qua non for the relationship of "persons acting in concert" to come into being.

In relation to trade name usage agreement between the taxpayer and its AE, the Delhi HC further rightly pointed out the fact that though the taxpayer had no rights over the trade name, and the manner of use of the trade mark had to be approved by the AE yet the taxpayer was under no obligation, contractual or otherwise, to

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incur expenditure towards building the brand of Whirlpool USA. It was further contended that the tax department was not able to put forth any argument towards the collusion between the AE i.e., Whirlpool USA and the taxpayer that owing to which taxpayer might have spent excessive amounts towards promotion of the brand of Whirlpool USA and why any incidental benefit, whatsoever, inuring to the AE should call for recovery of the same from the AE.

In light of the above discussions, the Delhi HC held that in the absence of an actual international transaction between the AE and the taxpayer, it cannot be established that an international transaction exists merely based on the carrying out of a ratio exercise between AMP expenditure incurred and revenues derived by the business. The Apex Court has declined the acceptance of the SLP filed by the income tax authority against the decision of the Delhi HC negating the existence of the international transaction in case of AMP expenses.

Reader's focus:

A lot of times it is observed that though the transfer pricing study emanates from the

business and operational aspects of a commercial activity which are carried out considering the circumstances prevailing at that point in time yet the advisors, consultants, tax authorities and related stakeholders affected by the transfer pricing regulations pivot or rush towards the prices or profitability of the controlled transactions which are subject to scrutiny.

It is very important to understand the intent as well as the follow-up actions and the results emanating out of the business transactions. Specifically considering the AMP expenditure controversy which has been prolonging since the last decade is based on a surmise i.e., the proposition of excess AMP expenditure when compared to other businesses. If this were to hold true, then it might open a Pandora's box in every case involving international transactions in nature of goods, services, intangibles, capital financing as the various activities comprising of budgeting, manufacturing, procurement, logistics, financing, distribution and any other business function are inter linked and thereby a blanket approach of ratio setting would lead to absurd results even within the same industry.

Therefore, it becomes important on part of the examiner to assess whether a controlled transaction actually exists as the determination of the admissibility of excess, or a shortfall based on the industry trends lacks the completeness of information which is not available in public domain.

Facts are the fuse conductors to the acceptance of the precedence in current year

Renishaw Metrology Systems Ltd [ITA No. 0628/Pune/2021- Order dated 26 November 2024 (Pune ITAT)]

The taxpayer is engaged in manufacturing of arms & cables and had entered into international transactions in the nature of software development services and marketing support services with its associated enterprises. The taxpayer's case was selected for scrutiny by TPO which made an upward adjustment in respect of the marketing support services employing the TNMM method. Aggrieved by the TPO's order, the taxpayer made an appeal before the CIT(A) which granted partial relief to the taxpayer by excluding certain comparable companies from the final set.

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Aggrieved by the CIT(A) ruling, the income tax department preferred an appeal before the Pune Tribunal for wrongful rejection of the comparable companies by the CIT(A) which was based on the stand taken by the predecessor CIT(A).

In this regard, one of the peculiarities which the Pune Tribunal stressed upon is the mere statement by the CIT(A) which contended that the comparables have been excluded in the preceding orders based on the functionality and other relevant factors and as a result ought to be excluded from the set of companies for the year under consideration. The Pune Tribunal held that though the CIT(A) has placed its reliance on the previous order by its predecessor yet the facts which ought to have been analysed to claim that the facts remain same have not been presented by the taxpayer and have neither been appreciated by the CIT(A) for the year under consideration. This was more specifically in light of testing the acceptance of the turnover filter which formed the very basis of rejection in preceding year as well as the year under consideration. Since the taxpayer was not able to demonstrate the difference in turnover of the

comparables vis-à-vis its own due to lack of factual data in the submission before the tax authorities and accordingly, the Pune Tribunal allowed the tax department to consider the companies as comparable.

Date of dispatch of email to be considered for the purpose of serving the notice

Hyundai Rotem Company Indian Project Offices [ITA No. 2027/Del/2022- Order dated 18 November 2024 (Delhi ITAT)]

The taxpayer was a Korea based company which was engaged in manufacturing railway vehicles and had entered into certain international transactions. The taxpayer's case was selected for transfer pricing scrutiny and the TPO made upward adjustments to the income of the taxpayer. Aggrieved by the TPO's actions, the taxpayer called for directions from the office of the Hon'ble DRP which passed its order on May 24, 2022.

The DRP's directions were received by the ACIT (International Taxation), Delhi on June 01, 2022 in physical form and the same was reflecting in the AO's worklist only on June 30, 2022. The Department contended that there was no

communication in relation to the DRP order which was emailed to the office of the ACIT(International Taxation), Delhi.

In this regard, the Delhi Tribunal held that the ignorance on part of the income tax department with respect to the email received on the designated email address cannot be the basis for the delay in passing the order by the AO. The Delhi Tribunal put forth its reliance on the Information Technology Act, 2000 wherein it provides that the dispatch of a record occurs when it enters a computer resource outside the control of the originator. The time of receipt of the electronic record is fixed by the provisions of sub-section (2) of Section 13 of the Information Technology Act, 2000. When the addressee has designated a computer resource, receipt occurs when the record enters the computer resource so designated. Accordingly, the date of receipt of the notice via email would be regarded as the date of dispatch i.e., May 24, 2022 and accordingly, the Delhi Tribunal held that the due date for passing the order by the AO would be June 30, 2022 instead of July 31, 2022.

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Extension of safe harbour rules for AY 2024-25 and inclusion of rough diamond trading under Safe Harbour Regime

[Notification No. 124/2024/ F. No. 370142/13/2024-TPL(Part) – Notification dated 29 November 2024]

CBDT, vide recent notification no 124 of 2024 dated 29 November, 2024, has extended the application of the Safe Harbour Rules to the assessment year 2024-25 (previous year 2023-24) as well. As per the circular 18 of the 2024, the CBDT has extended the due date of filing tax return to 15 December, 2024 and as a result, the taxpayers who are otherwise to going to file the transfer pricing report under section 92E of the ITA may choose to make an application under the Safe Harbour provisions.

Further, in addition to the vanilla extension of the Safe Harbour provisions, in order to provide a boost to the diamond corridor of Gujarat and Maharashtra, CBDT has expanded the scope of the safe harbour provisions to foreign diamond mining companies engaged in trading of raw diamonds in the notified zones covered by clause (e) of Explanation 1 to section 9(1)(i) of

the ITA. CBDT has allowed the umbrella of the Safe Harbour provisions to those rough diamond trading entities whose income chargeable to profit and gains from business or profession shall be 4 percent or more of the gross receipts from the raw diamond trading business.

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GST Portal Updates and Advisory

Advisory for Reporting TDS Deducted by scrap Dealers in October 2024

Registered persons receiving supplies of metal scrap classified under Chapter 72 to 81 of the Customs Tariff Act, 1975 are mandated to deduct GST TDS u/s 51 of the CGST Act 2017, with effect from October 10, 2024¹

Taxpayers who applied for GST registration in October 2024 but were approved in November 2024 encountered issues in reporting TDS deducted for the month of October 2024, as the GST system did not allow filing for periods before the registration month.

To resolve this, the GSTIN has issued an advisory that taxpayers are advised to report the consolidated TDS deducted from October

10,2024 to November 30, 2024, in the GSTR-7 return for the month of November 2024.

Advisory on GSTR 2B and IMS

It has been observed that in a few cases, the GSTR-2B for the month of October 2024 has not been generated. In this regard, the GSTN has issued an advisory stating that the GSTN portal will not generate GSTR-2B in the following scenarios:

- (i) **QRMP Scheme Filers:** Taxpayers under the Quarterly Return Monthly Payment (QRMP) scheme will not receive GSTR-2B for the first two months of a quarter. For the October-December 2024 quarter, GSTR-2B will only be available for December, not for October or November.
- (ii) **Pending GSTR-3B Filings:** GSTR-2B will not be generated if the taxpayer has not filed the previous period's GSTR-3B.

For instance, if GSTR-3B for September 2024 is pending, GSTR-2B for October 2024 will not be generated. The taxpayer must file the pending GSTR-3B and then manually compute GSTR-2B

for October 2024 using the "Compute GSTR-2B" button on the IMS dashboard.

Advisory regarding IMS during initial phase of its implementation

In October 2024, the GST Portal introduced an optional Invoice Management System (IMS). This allows recipients to manage invoices reported by suppliers in GSTR-1/1A/IFF by accepting, rejecting, or keeping them pending. The recipient's actions on IMS determine the details of GSTR-2B, generated on the 14th of the following month.

Taxpayers can verify invoices on IMS, affecting the availability of ITC in GSTR-2B. Rejected invoices will not be available for ITC. GSTR-3B will also have auto-populated liabilities and ITC from GSTR-1/1A and GSTR-2B, but taxpayers can still edit these details before filing.

During the initial phase, recipients may make mistakes, leading to incorrect ITC or liability details in GSTR-3B.

In this regard, the GSTIN has issued an advisory that taxpayers can correct such errors in IMS before filing GSTR-3B. If errors persist,

¹ refer KCM Insight for the month of October 2024

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taxpayers are advised to manually edit GSTR-3B to ensure accuracy.

Advisory for waiver scheme under section 128A

The GSTN has issued clarificatory advisory on November 8, 2024 for taxpayers who are willing to opt for waiver scheme under Rule 164 of CGST Rules, 2017 which is notified effective November 1, 2024. The advisory states that the relevant forms GST SPL-01 and GST SPL-02 are under development and the same will be made available on GSTN tentatively from first week of January, 2025.

In the meantime, taxpayers are advised to make payment of tax as per demand or order through DRC-03 and if payment has already been made through Form GST DRC-03 for any demand order, taxpayers need to link it to the demand order using Form GST DRC-03A, which is now available on the common portal.

Advisory for Form GST DRC-03A

The GSTN has issued an advisory dated November 5, 2024, mentioning that the

taxpayers have paid the demands through DRC-03 instead of using the 'Payment towards demand' facility on the GST portal, resulting the demand not being closed in the electronic liability register.

To resolve this, the government has introduced Form GST DRC-03A via Notification No. 12/2024 on July 10, 2024 which allows adjustment of amounts paid through DRC-03 against the corresponding demand order.

Vide this advisory, it is advised to the taxpayers to use the DRC-03A form to link the payment made vide DRC-03 with the demand order. Only DRC-03 forms where the cause of payment is either 'Voluntary' or 'Others' can be used in the Form GST DRC-03A.

The taxpayers need to enter the ARN of the DRC-03 along with the demand order number on the portal and the system will auto-populate relevant information from both the DRC-03 form and the demand order. Once the adjustment was made, entries will be posted automatically in the taxpayer's liability ledger to reflect the updated demand status. In case of technical issues, taxpayers should raise a ticket

under the 'DRC-03A-Filing' category on the Grievance Redressal Portal.

Advisory on Time Limit for Reporting e-Invoice on the IRP Portal

The GSTIN has issued an advisory stating that, effective from April 01, 2025, taxpayers with an Annual Aggregate Turnover (AATO) of ₹10 crores and above must report e-Invoices to the Invoice Registration Portal (IRP) within 30 days of the invoice date.

This requirement applies to all document types, including invoices, credit notes, and debit notes.

Previously, this 30-day reporting time limit applied to taxpayers with an AATO of ₹100 crores and above. Starting from 1st April 2025, taxpayers meeting the revised threshold of ₹10 crores will be prohibited from reporting e-Invoices older than 30 days. However, it is clarified that, no restrictions apply for taxpayers with an AATO below ₹10 crores as of now.

For example, an invoice dated 1st April 2025 must be reported by 30th April 2025.

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**Pre deposit can be made through Electronic Credit Ledger when filing appeals u/s 107(6) of the CGST Act***[WP(C)/35488 of 2023– Madras HC]*

The petitioner, engaged in manufacturing and supplying passenger vehicles, filed GST returns periodically. The department issued a notice alleging a differential GST liability based on differences between GSTR-1 and GSTR-3B returns for FY 2017-18. Upon receiving an adverse order, petitioner filed an appeal after paying 10% of the disputed tax using its Electronic Credit Ledger, as per the procedure u/s 107(6) of the CGST Act.

The Office of the Joint Commissioner issued a Deficiency Memo, stating that the pre-deposit had to be made through the Electronic Cash Ledger rather than the Electronic Credit Ledger. The petitioner then challenged the validity of this Deficiency Memo.

The petitioner argued that section 107(6) of the CGST Act allows for the pre-deposit of disputed tax. Section 49(4) of the CGST Act permits utilization of the Electronic Credit Ledger for payment of output tax. Rule 86(2) of the CGST

Rules also allows for debiting the Electronic Credit Ledger for the discharge of liability. The petitioner further referenced CBIC Circular No.172/04/2022-GST, which clarifies that the pre-deposit of 10% tax can be paid using the Electronic Credit Ledger.

The respondent argued that the pre-deposit requirement u/s 107(6) does not equate to output tax and must be paid through the Electronic Cash Ledger, as specified u/s 49. They contended that the utilization of the Credit Ledger is limited to payment of output tax and does not extend to pre-deposits for filing appeals.

The Madras High Court allowed the writ petition and quashed the Deficiency Memo. The court held that section 107(6) of the CGST Act does not explicitly prohibit the use of the Electronic Credit Ledger for pre-deposits. Further, it noted that both section 49(4) and the CBIC Circular support the use of the Credit Ledger for output tax and pre-deposits. The court directed the respondent to accept the appeal with the pre-deposit paid through the Electronic Credit Ledger and proceed with the hearing.

The ruling confirms that taxpayers are entitled to use the Electronic Credit Ledger for making a pre-deposit of 10% of the disputed tax when filing appeals u/s 107(6) of the CGST Act, except for the payment involving reverse charge mechanism.

Inadvertent procedural error in splitting IGST into CGST and SGST does not constitute wrongful availment of input tax credit*[WA No. 54 of 2024 – Kerala HC]*

The appellant incorrectly recorded the IGST component as nil in GSTR-3B, instead bifurcating it into CGST and SGST credits. This led to a mismatch between GSTR-2A and GSTR-3B, The Assessing Authority issued a notice alleging that the appellant utilized 'unavailable credit' and demanded the repayment of CGST and SGST used in excess.

The appellant argued that the misrepresentation of IGST as CGST and SGST in Form GSTR-3B was an inadvertent error made during filing, without any intention to defraud or evade taxes. It was further submitted that the IGST credit had been fully paid by the supplier,

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and the same was merely allocated incorrectly due to the absence of outward supplies that attracted IGST during that period.

The appellant further contended that since there was no excess utilization or misappropriation of tax credit, there was no resulting revenue loss

The Assessing Authority issued a demand notice for the recovery of wrongly utilized CGST and SGST credits, arguing that the appellant had incorrectly split the IGST paid on inward supplies into CGST and SGST components instead of showing it as IGST credit in Form GSTR-3B. The department contended that this incorrect representation violated the proper utilization procedures mandated under GST law, which specifically prescribe that IGST must first be utilized for IGST liabilities before being split into CGST and SGST components. The department maintained that this misrepresentation deprived the State of its legitimate share of the IGST and could potentially lead to compliance gaps if not corrected.

The High Court ruled in favour of the appellant, recognizing the procedural mistake as a technical oversight without substantive consequences. The Court found that the appellant did not gain any undue benefit and that no actual revenue loss had occurred. It further clarified that the proceedings u/s 73 of the GST Act were unnecessary since the appellant had not wrongfully availed or utilized any excess credit. The Court also highlighted that such technical errors, when they do not impact revenue collection or result in any malfeasance, should be treated with a sense of fairness.

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Important Updates - RBI

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

RBI/2024-2025/87 DOR.AML.REC.49/14.01.001 /2024-25 dated November 06, 2024

Regulated Entities ('REs'), implying banks and financial institutions, have to undertake Customer Due Diligence ('CDD') on a periodic basis of their customers on a laid down process to ensure transparency and good governance. To ease the process for the customers, the CDD will now be undertaken at Unique Customer Identification Code ('UCIC') level so that for an existing KYC compliant customer desirous to open another account or avail any other product or service from the same Regulated Entity will not be required to undertake a fresh CDD exercise.

Explanation: A Unique Customer Identification Code ('UCIC') is an alphanumeric code assigned to each customer by the financial institutions. This code serves as distinct identifier for the customer, facilitating seamless tracking and management of their account. It helps in consolidating customer data, enabling banks to

maintain accurate records and monitor account activities effectively.

There are other guidelines such as more intensified monitoring for accounts designated as high risk, explanation to periodic updation of KYC and sharing KYC information with Central KYC Records Registry ('CKYCR').

Effective date: Immediate effect

'Fully Accessible Route' for Investment by Non-residents in Government Securities – Inclusion of Sovereign Green Bonds

RBI/2024-25/88 FMRD.FMD.No.06/14.01.006/ 2024-25 dated November 07, 2024

The Reserve Bank, in consultation with the Government of India, vide A.P. (DIR Series) Circular No. 25 dated March 30, 2020, had introduced a separate channel, called the 'Fully Accessible Route' (FAR), which enabled non-residents to invest in specified Government of India dated securities ('specified securities'). Eligible investors can invest in specified Government securities without being subject to any investment ceilings.

It has now been decided to also designate the Sovereign Green Bonds of 10-year tenor issued by the Government in the second half of the fiscal year 2024-25 under the category of 'specified securities' for investment under the FAR.

Effective date: Immediate effect

Operational framework for reclassification of Foreign Portfolio Investment to Foreign Direct Investment

RBI/2024-25/90 A.P. (DIR Series) Circular No. 19 dated November 11, 2024

RBI has notified the operational framework for reclassification of Foreign Portfolio Investment to FDI wherein specific timelines have been prescribed for either divesting the holding so as to reduce below the threshold limit or to undertake necessary reporting compliances for the FPI holding to be redesignated as FDI holding, in case the investor proposes to continue to hold such investment.

A detailed explanation on the operational guidelines notified by the Reserve Bank of India

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has been shared in form of *KCM Flash* released on November 21, 2024.

Effective date: Immediate effect

Directions for Central Counterparties (CCPs)

RBI/2024-2025/85 DPSS.CO.RLVPD.No.5789/02.07.038/2024-25 dated October 28, 2024

RBI has been prescribing directions related to capital requirements and governance framework for Central Counterparties ('CCPs') along with providing a framework for recognition of foreign CCPs under the Payment and Settlement Systems Act, 2007 ('PSS') since Yr. 2019. Based on a periodic review of the directions for CCPs, the RBI has updated directions governing the functioning of CCPs.

Explanation: A Central Counterparty ('CCP') is a clearing house that interposes itself between counterparties to contracts traded in one or more financial markets, becoming the buyer to every seller and the seller to every buyer and thereby ensuring the future performance of open contracts. A CCP becomes counterparty to trades with market participants through novation, an open offer system, or another

legally binding arrangement. For the purposes of the capital framework, a CCP is a financial institution.

It thus implies that CCP has a vital role to play in the whole PSS infrastructure by not only acting as an intermediary for trade between the buyer and seller but more importantly acts as a guarantor for every trade.

The directions notified provide guidelines for not only domestic CCPs but also for CCPs registered outside India, wherein the Act does not differentiate between domestic and foreign entities.

The guidelines provided in the directions cover the following aspects for CCPs, including:

- Composition of Board and roles and responsibilities of its key management personnel
- Guidelines on various committees including:
 - Nomination and Remuneration Committee
 - Risk Management Committee

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- Audit Committee
- Technical Committee
- Disclosures and conflict of interest
- Net worth and ownership parameters including eligibility and holding of shares in the CCP
- Specific additional guidelines for foreign CCPs, including methodology for application to RBI for grant of recognition as CCP and other organizational requirements.

Effective date: Immediate effect

Important Updates - SEBI

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Clarification with respect to advertisement code for Research Analysts (RAs)

SEBI/HO/MIRSD/MIRSD-PoD1/P/CIR/2024/146 dated October 24, 2024

SEBI vide its Circular in April 2023 and Master Circular in May 2024 had issued specified provisions related to advertisement code to be followed by a Research Analyst ('RA') in their advertisements.

Based on clarifications sought on the advertisement code, SEBI has clarified that Research Report and research recommendations of RA are not considered advertisement unless anything contained in the research report is in the nature of promotion of products or services offered by RA.

The advertisement code shall be applicable to all forms of communication including:

- printed media or displays like sign boards/hoarding; or
- electronic, wired, or wireless communication, such as electronic mail, text messaging, messaging platforms, social media platforms; or

- audio-visual form of communication, including television, video tape recordings, motion pictures or;
- in any other manner whatsoever.

SEBI has further clarified that a research report, irrespective of the mode of dissemination will be construed as an advertisement if anything contained in the research report, either expressly or implicitly promotes products or services offered by the RA.

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

SEBI/HO/IMD/IMD-PoD-1/P/CIR/149 dated November 04, 2024

Mutual Funds were permitted by SEBI to invest in overseas securities vide Master Circular dated June 27, 2024, which included investment in overseas Mutual Funds/Unit Trusts ('MF/UTs'). However, to ensure that the overseas MF/UTs were not ploughing back the funds to Indian securities market, certain guidelines have been provided for such investments, including:

- At the time of making investments (both fresh and subsequent), Indian Mutual Fund schemes will have to ensure that the

underlying overseas MF/UTs do not have more than 25% exposure to Indian securities.

- Subsequent to the investment, if the exposure by an underlying overseas MF/UTs to Indian securities exceeds 25% of their net assets, there will be a 6-month observance period, where no further investment will take place from the Indian Mutual Fund scheme.
- If the portfolio of an underlying overseas MF/UT is not rebalanced during the 6-month observance period, Indian Mutual Fund scheme shall liquidate its investments in the said overseas MF/UT within the next 6 months ('liquidation period') from end of the observance period.

Applicability:

Immediate Effect

Disclosure of expenses, half yearly returns, yield and risk-o-meter of schemes of Mutual Funds

SEBI/HO/IMD/PoD1/CIR/P/2024/150 dated November 05, 2024

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To facilitate enhanced transparency, ease of understanding by the mutual fund investors and bringing about a standardised approach towards disclosures by the Mutual Fund industry, the following recommendations of the Mutual Fund Advisory Committee have been decided to be introduced:

A. Disclosure of expenses, half yearly returns and yield of a scheme

- Total recurring expenses for Direct plan (which are generally lower since client directly invests in a particular scheme) and Regular plan (where a client invests in a scheme through an intermediary, generally a broker, MF distributor or a bank), apart from the disclosure of total recurring expenses of the scheme.
- Separate disclosures of returns during the half year and compounded annualized yields respectively for direct and regular plans.

To standardise the above disclosures, the format for half-yearly financial statement for MF schemes will be reviewed and finalised by Association of Mutual Funds of India ('AMFI'), in consultation with SEBI.

B. Colour Scheme for Risk-o-meter

- Risk-o-meter shall have six different colour levels for indicating risk for mutual funds, ranging from Low risk to Very High Risk, each being assigned a unique colour code.
- The colour scheme of risk-o-meter will be applicable for all digital and polychrome printed promotion materials / disclosures for the schemes.
- 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.

Applicability:

With effect from December 05, 2024

Trading supported by Blocked Amount in Secondary Market

SEBI/HO/MRD-PoD2/CIR/P/2024/153 dated November 11, 2024

For trading in secondary market, a client had to transfer funds upfront to the account of the Trading Members ('TMs') where they had their

trading account for any purchase of equity shares. To provide greater security for the investors' funds, SEBI in October 2023, introduced a supplementary process of blocking funds in investors' bank account instead of transferring the same to the Trading Members' account.

To provide safeguards to trading by the clients, in addition to the already existing system of transferring funds to the account of the Trading Member, the Qualified Stock Brokers (QSBs) have now been mandated to provide their clients with two additional options (i.e.):

- the facility of trading supported by blocked amount in the secondary market (cash segment) using UPI block mechanism; or
- the 3-in-1 Trading Account facility, which is primarily the integration of the trading account with the demat and bank accounts of the client.

Applicability:

Effective from February 01, 2025

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**Procedure for reclassification of FPI investment to FDI**

*SEBI/HO/AFD/AFD-POD-3/P/CIR/2024/152
dated November 11, 2024*

Regulations 20(7) and 22(3) of the SEBI (Foreign Portfolio Investors) Regulations, 2019 provided that in case a FPI failed to divest its holdings (in excess of the prescribed threshold), within five trading days, the entire investment in the company by such foreign portfolio investor including its investor group would be considered as investment under the category of FDI.

RBI has provided operational guidelines for reclassification of FPI to FDI in case of breach is continued by such FPI as well as the procedure for divestment to reduce the holding below the threshold limit prescribed vide its Circular RBI/2024-25/90 A.P. (DIR Series) Circular No. 19 dated November 11, 2024.

Applicability:

Immediate effect

Withdrawal of Master Circular on issuance of No Objection Certificate (NOC) for release of 1% of Issue Amount

*SEBI/HO/CFD/CFD-PoD-2/P/CIR/2024/0161
dated November 21, 2024*

To streamline processes and to facilitate ease of doing business to an Issuer company, the requirement to deposit 1% of the issue size available for subscription to the public with the designated stock exchange by the Issuer company has been done away with.

As a consequence, the issuance of No Objection Certificates (NOCs) required for releasing the 1% deposit as per the Master Circular dated November 7, 2022 also stands withdrawn. Stock exchanges have been given instructions to implement standard operating procedure (SOP) for release of such 1% deposits submitted prior to the aforesaid amendment.

Applicability

Immediate Effect

Guidelines to Stock Exchanges, Clearing Corporations and Depositories

*SEBI/HO/MRD/POD-3/P/CIR/2024/162 dated
November 22, 2024*

Indian stock market capitalization (combined for both National Stock Exchange and Bombay Stock Exchange) stands in excess of USD 5 trillion, being the fourth largest in terms of market cap, behind USA, China, and Japan. The continuous growth in the stock market is not only led by the increase in valuation of the existing stocks trading in the secondary market but also the slew of primary market issues ranging from new public offerings from not only new age businesses but also from sectors such as automobile and manufacturing to chemicals and pharmaceuticals. All this puts a every increasing responsibility and accountability on the market infrastructure institutions ('MII's') i.e., Stock Exchanges, Clearing Corporations and Depositories, whose role keeps on increasing and expanding with the growing stock market.

To ensure that the MIIs keep pace with the booming markets, guidelines are issued from

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time to time. In continuation of such guidelines at regular intervals, and on the basis of recommendations of the Committee on Strengthening of Governance of MII and subsequent deliberations in the Industry Standards Forum (ISF), the following guidelines have been issued to MII:

- Mechanism to enhance Accountability, including meetings of Public Interest Directors ('PIDs'), quarterly reporting by Compliance Officer, Half yearly reporting by Chief Risk Officer, Whistle Blower Policy for MII etc.
- Enhancing Supervision and Monitoring Mechanism of MII through Regulatory Technologies ('RegTech') and Supervisory Technologies ('SupTech').
- Training or knowledge up-gradation of Directors on Governing Board of MII by providing at least seven days of training in a year to all its Directors.
- Policy on Data Sharing by MII by having an internal policy for sharing and monitoring of confidential and sensitive data, reviewing its effectiveness annually

by Standing Committee on Technology (SCOT) and reporting of non-compliances within a specified time period.

- Appointment or Reappointment of Directors on the Governing Board wherein the MII shall submit brief profiles of at least two prospective candidates to SEBI, develop a skill evaluation metrics to assess the applications for appointment or reappointment of PIDs and to take the help of an independent Human Resource ('HR') Agency to independently collect/verify the information.
- Reporting lines of KMPs - SEBI has mandated MII to have certain KMPs including;
 - Compliance Officer ('CO') responsible for the Compliance function
 - Chief Risk Officer ('CRiO') responsible for identification and mitigation of risks being faced by the MII

- Chief Technology Officer ('CTO') responsible for the organization's overall technology strategy, innovation, and technical infrastructure and;
- Chief Information Security Officer ('CISO') responsible for safeguarding data and information through cybersecurity practices.

Applicability:

April 01, 2025

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For detailed understanding or more information, send your queries to knowledge@kcmehta.com

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Independent Member



Abbreviations

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Abbreviation	Meaning
AA	Advance Authorisation
AAR	Authority of Advance Ruling
AAAR	Appellate Authority of Advance Ruling
AAC	Annual Activity Certificate
AD Bank	Authorized Dealer Bank
AE	Associated Enterprise
AGM	Annual General Meeting
AIR	Annual Information Return
ALP	Arm's length price
AMT	Alternate Minimum Tax
AO	Assessing Officer
AOP	Association of Person
APA	Advance Pricing Arrangements
AS	Accounting Standards
ASBA	Applications Supported by Blocked Amount
AY	Assessment Year
BAR	Board of Advance Ruling
BEAT	Base Erosion and Anti-Avoidance Tax
CBDT	Central Board of Direct Tax
CBIC	Central Board of Indirect Taxes and Customs
CCA	Cost Contribution Arrangements
CCR	Cenvat Credit Rules, 2004
COO	Certificate of Origin

Abbreviation	Meaning
CESTAT	Central Excise and Service Tax Appellate Tribunal
CGST Act	Central Goods and Service Tax Act, 2017
CIT(A)	Commissioner of Income Tax (Appeal)
Companies Act	The Companies Act, 2013
CPSE	Central Public Sector Enterprise
CSR	Corporate Social Responsibility
CTA	Covered Tax Agreement
CUP	Comparable Uncontrolled Price Method
Customs Act	The Customs Act, 1962
DFIA	Duty Free Import Authorization
DFTP	Duty Free Tariff Preference
DGFT	Directorate General of Foreign Trade
DPIIT	Department of Promotion of Investment and Internal Trade
DRI	Directorate of Revenue Intelligence
DRP	Dispute Resolution Panel
DTAA	Double Tax Avoidance Agreement
ECB	External Commercial Borrowing
ECL	Electronic Credit Ledger
EO	Export Obligation
EODC	Export Obligation Discharge Certificate

Abbreviation	Meaning
EPCG	Export Promotion Capital Goods
FDI	Foreign Direct Investment
FEMA	Foreign Exchange Management Act, 1999
FII	Foreign Institutional Investor
FIFP	Foreign Investment Facilitation Portal
FIRMS	Foreign Investment Reporting and Management System
FLAIR	Foreign Liabilities and Assets Information Reporting
FPI	Foreign Portfolio Investor
FOCC	Foreign Owned and Controlled Company
FTC	Foreign Tax Credit
FTP	Foreign Trade Policy 2015-20
FTS	Fees for Technical Service
FY	Financial Year
GAAR	General Anti-Avoidance Rules
GDR	Global Depository Receipts
GMT	Global Minimum Tax
GILTI	Global Intangible Low-Taxed Income
GSTN	Goods and Services Tax Network
GVAT Act	Gujarat VAT Act, 2006
HSN	Harmonized System of Nomenclature

Abbreviations

Abbreviation	Meaning
IBC	Insolvency and Bankruptcy Code, 2016
ICDS	Income Computation and Disclosure Standards
ICDR	Issue of Capital and Disclosure Requirements
IEC	Import Export Code
IIR	Income Inclusion Rule
IMF	International Monetary Fund
IRP	Invoice Registration Portal
IRN	Invoice Reference Number
ITC	Input Tax Credit
ITR	Income Tax Return
IT Rules	Income Tax Rules, 1962
ITAT	Income Tax Appellate Tribunal
ITR	Income Tax Return
ITSC	Income Tax Settlement Commission
JV	Joint Venture
LEO	Let Export Order
LIBOR	London Inter Bank Offered Rate
LLP	Limited Liability Partnership
LOB	Limitation of Benefit
LODR	Listing Obligations and Disclosure Requirements
LTA	Leave Travel Allowance
LTC	Lower TDS Certificate

Abbreviation	Meaning
LTCG	Long term capital gain
MAT	Minimum Alternate Tax
MCA	Ministry of Corporate Affairs
MeitY	Ministry of Electronics and Information Technology
MSF	Marginal Standing Facility
MSME	Micro, Small and Medium Enterprises
NCB	No claim Bonus
OECD	The Organization for Economic Co-operation and Development
OM	Other Methods prescribed by CBDT
PAN	Permanent Account Number
PE	Permanent establishment
PPT	Principle Purpose Test
PSM	Profit Split Method
PY	Previous Year
QDMTT	Qualified Domestic Minimum Top-up Tax
RA	Regional Authority
RMS	Risk Management System
ROR	Resident Ordinary Resident
ROSCTL	Rebate of State & Central Taxes and Levies
RoDTEP	Remission of Duties and Taxes on Exported Products

Abbreviation	Meaning
RPM	Resale Price Method
SC	Supreme Court of India
SCN	Show Cause Notice
SDS	Step Down Subsidiary
SE	Secondary adjustments
SEBI	Securities Exchange Board of India
SEP	Significant economic presence
SEZ	Special Economic Zone
SFT	Specified Financial statement
SION	Standard Input Output Norms
SOP	Standard Operating Procedure
ST	Securitization Trust
STCG	Short term capital gain
SVLDRS	Sabka Vishwas (Legacy Dispute Resolution Scheme) 2019
TCS	Tax collected at source
TDS	Tax Deducted at Source
TNMM	Transaction Net Margin Method
TP	Transfer pricing
TPO	Transfer Pricing Officer
TPR	Transfer Pricing Report
TRO	Tax Recovery Officer
UTPR	Undertaxed Profits Rules
u/s	Under Section
WOS	Wholly Owned Subsidiary

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