Foreign Portfolio Investors

Tax and Regulatory Updates – India 2019

1 February 2020

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1. Regulatory Updates - (1 February 2019 till date)

**New FPI regulatory framework**

- **Report of working group on FPI Regulations, 2014 published for comments**
  In March 2018, Securities and Exchange Board of India (SEBI), had constituted a Working Group (WG) under the chairmanship of Harun R. Khan, former Deputy Governor of Reserve Bank of India (RBI) to revamp and redraft Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2014 (FPI Regulations, 2014).
  The objective of the WG was to review and present a comprehensive framework of regulations, simplify the regulations and improve consistency, rationalize and liberalize the investment rules, and review the Know Your Client (KYC) requirements.
  The WG held consultations with various stakeholders and arrived at certain recommendations. SEBI published report of WG seeking public comments by 14 June 2019.
  The key recommendations included, inter alia, fast tracking on-boarding process for select Category II Foreign Portfolio Investors (FPI), simplified registration for Multiple Investment Managers (MIM) structures, pension fund to be considered for Category I FPI registration, review of broad based condition for appropriately regulated entities, deemed broad based status for insurance/ re-insurance entities, strengthening of Offshore Derivative Instruments (ODI) framework etc.
  Source: Report of working group on SEBI (Foreign Portfolio Investors) Regulations, 2014 submitted by the working group under the Chairmanship of Shri Harun R. Khan, Deputy Governor (retd.), Reserve Bank of India dated 24 May 2019

- **Review of SEBI (FPI) Regulations 2014**
  SEBI Board held a meeting on 21 August 2019 in Mumbai where it, inter alia, approved new set of FPI regulations after considering the recommendations of the WG chaired by Mr. H.R.Khan submitted earlier.
  The key focus was to simplify and rationalize the existing regulatory framework for FPIs in order to ease the operational constraints and compliance requirements.
  Source: SEBI Board Meeting PR 20/2019 dated 21 August 2019

- **SEBI (FPI) Regulations, 2019 notified - 23 Sep 2019**
  SEBI notified the Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2019 (‘FPI Regulations 2019’) on 23rd September 2019. This superseded the SEBI (FPI) Regulations, 2014.
  Key areas covered in the aspects of the FPI Regulations, 2019 are:
  - Re-categorization of FPI categories into two categories
  - Relaxed eligibility criteria for FPI registration
  - Offshore Derivative Instruments
  - Need to obtain FPI registration
  - Investment avenues
  - Transactions where brokers not needed by FPI
  - Process of divestment
  Source: Securities and Exchange Board of India (Foreign Portfolio Investors) Regulation, 2019

- **SEBI issued operational guidelines for FPIs - 5 Nov 2019**
  SEBI issued operational guidelines (OG) for FPI and DDPs under FPI Regulations, 2019 and for Eligible Foreign Investors (EFI) on 5 November 2019.
  The guidelines were issued to ensure efficient transition from erstwhile FPI Regulations, 2014. The prevailing circulars, FAQs, OG, other guidance issued by SEBI stood withdrawn.
The sections covered under the OG are

- **FPI registration related activities** - dealing with change in the category of FPIs upon notification of Regulations, processing of FPI applications, for entities as such bank and subsidiary of bank applicant, insurance and re-insurance, pension funds, appropriately regulated entities investing on behalf of clients, etc.

- **KYC for FPIs** - FPIs to provide KYC related documents based on the category under which they are registered. The documents to be uploaded on KYC Registration Agencies (KRA) portal for other market intermediaries to access and complete their KYC requirements.

- **Investment Conditions / Restriction on FPIs** - providing positions limits for stock and stock index derivative contracts, mechanism for write-off of securities, eligibility for investment in ‘to be listed’ corporate debts.

- **ODI** - providing conditions for issuance of ODI, registration and compliance, KYC of subscribers.

- **Participation/functioning of EFIs in International Financial Services Centre (IFSC).**

- **Changes in FPI application form**

Source: SEBI circular IMD/FPI&C/CIR/P/2019/124 dated 5 November 2019

❖ **Exemption from clubbing of investment limit for foreign Government agencies and its related entities**

SEBI amended Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2019 and operational guidelines, by exempting certain foreign government agencies and their related entities from clubbing requirements and other investment conditions, either by way of an agreement or treaty with other sovereign government, or by an order of the central government.

This is in line with Schedule II (Investments by Foreign Portfolio Investors) Foreign Exchange Management (Non-debt Instruments) Rules, 2019.


❖ **Framework for issue of Depository Receipts w.e.f 10 October 2019**

SEBI provided a framework for issue of Depository Receipts (‘DR’) w.e.f 10 October 2019. This supplements the DR scheme of 2014. The framework applies to DRs issued (post 10 October 2019) by a company incorporated in India and listed on a Recognized Stock Exchange in India’ (‘Listed Company’).

The key aspects of the framework are as under:

- **Specific terms** such as DR, permissible securities, foreign depository defined.

- **Permissible holder of DR** means holder of DR including its beneficial owner (BO). Resident of India and Non-Resident Indian (NRI) not to be permissible holders.

- **Requirements/ Conditions**
  For issuance of DRs, a Listed Company may issue permissible securities, or their holders may transfer permissible securities.

- **Voting Rights:**
  Voting rights on permissible securities is to be exercised by DR holder through Foreign Depository pursuant to voting instruction only from DR holder.

- **Eligibility criteria for Listed Company**
  Listed Company to comply with requirements prescribed by SEBI. Listed Company eligible to issue Permissible Securities subject to condition such as Listed Company or its promoters or directors not debarred from accessing the capital market by SEBI, are not willful defaulter; are not fugitive economic offender etc.

- **Eligibility criteria for existing holders**
  To be eligible to transfer Permissible Securities; if the Listed Company or the holder transferring Permissible Securities are not debarred from accessing the capital market by SEBI; are not willful defaulter; are not fugitive economic offender etc.

- **Issue of Depository Receipts**
  Initial issue and listing of DRs - Listed Company to provide an opportunity to its equity share-holders to tender their shares for participation in such listing of DRs. Subsequent issue and listing of DRs may take place subject to limits approved.
Company can propose to make a public offer and list on RSE, and simultaneously propose to issue Permissible Securities or transfer Permissible Securities of existing holders on an International Exchange by seeking necessary approvals from RSE and International Exchange.

- **Permissible Jurisdictions and International Exchanges**

  Listed Company can issue Permissible Securities or transfer Permissible Securities of existing holders in Permissible Jurisdictions. The DRs to be listed on any of the specified International Exchange of the Permissible Jurisdiction as may be notified by SEBI.

  *Inter alia*, the circular also contains provisions relating to pricing of DRs, obligations of Listed Company, Indian Depository, Foreign Depository and Domestic Custodian.

  Source: SEBI circular SEBI/HO/MRD/DOP1/CIR/P/2019/106 dated 10 October 2019

- **SEBI issued circular listing permissible jurisdiction and international exchange**

  SEBI had earlier issued the framework for issuance of DRs by a Listed Company on 10 October 2019. As per the framework Listed company is permitted to issue / transfer permissible securities for the purpose of issue of DRs, only in permissible jurisdictions, and said DRs to be listed on any of the specified International Exchange of the Permissible Jurisdiction.

  In this regard, SEBI issued circular listing the permissible jurisdiction and international exchange. These include NASDAQ, NYSE, Tokyo Stock Exchange, Korea Exchange Inc. London Stock Exchange; Euronext Paris, Frankfurt Stock Exchange, Toronto Stock Exchange, India International Exchange, NSE International Exchange.

  Source: SEBI circular SEBI/HO/MRD2/DCAP/CIR/P/2019/146 dated 28 November 2019

- **FPI investment limit in corporate debt revised**

  In order to encourage wider spectrum of investors to access the Indian corporate debt market, RBI withdrew the condition that:

  - No FPI shall have an exposure of more than 20% of its corporate bond portfolio to a single corporate (including exposure to entities related to the corporate) w.e.f 15 February 2019.

  SEBI also stated that no separate circular is to be issued by it with respect to investment conditions for FPI Investment in corporate debt securities. FPIs required to comply with circulars and directions issued hereinafter by RBI in this regard.


- **FPI investments limits in debt securities revised**

  RBI provided various FPI limits in debt securities in March 2019. The existing and revised limits are:

<table>
<thead>
<tr>
<th>Type of instrument</th>
<th>Current Limits*</th>
<th>Revised Limits for the period Apr- Sep 2019*</th>
<th>Revised Limits for the period Sep – Mar 2020*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government Security (G- Sec) – General</td>
<td>2,233</td>
<td>2,347</td>
<td>2,461</td>
</tr>
<tr>
<td>G- Sec- Long Term</td>
<td>923</td>
<td>1,037</td>
<td>1,151</td>
</tr>
<tr>
<td>State Development Loan (SDL)- General</td>
<td>381</td>
<td>497</td>
<td>612</td>
</tr>
<tr>
<td>SDL- Long Term</td>
<td>71</td>
<td>71</td>
<td>71</td>
</tr>
<tr>
<td>Corporate Bonds</td>
<td>2,891</td>
<td>3,031</td>
<td>3,170</td>
</tr>
<tr>
<td>Total</td>
<td>6,499</td>
<td>6,983</td>
<td>7,465</td>
</tr>
</tbody>
</table>

  *Amounts in INR billions

  - Limit for FPI investment in G-secs, SDLs and corporate bonds to be 6%, 2%, and 9% of outstanding stocks of securities, respectively, in FY 2019-20

  - The allocation of increase in G-sec limit over the two sub-categories – ‘General’ and ‘Long-term’ – set at 50:50 for the year 2019-20. The entire increase in limits for SDLs added to the ‘General’ sub-category of SDLs.

  - Coupon reinvestment arrangement for G-Sec to be extended to SDLs

RBI and SEBI permit FPIs to invest in municipal bonds

In order to broaden access of non-resident investors in debt instruments in India, RBI permitted FPIs to invest in municipal bonds. Accordingly, SEBI amended FPI Regulations, 2014.

Municipal Bonds means debt instruments issued by municipalities constituted under Constitution of India. Such investments are to be reckoned within the limits set for FPI investment in SDL. All other existing conditions for investment by FPIs in the debt market remained unchanged.


RBI notified Foreign Exchange Management (Debt Instruments) Regulations, 2019

In supersession of the Foreign Exchange Management (Transfer of Issue of Security by a Person Resident outside India) Regulations, 2017 [FEMA 20(R)], RBI issued notification to regulate investment in India by a Person Resident Outside India.

The various aspects of the notification are:

- **Restriction on investment by a person resident outside India**
  
  No person resident outside India to make investment in India unless provided in FEMA.

- **Restriction on receiving investment**
  
  An Indian entity, mutual fund, venture capital fund, a firm, an association of persons or a proprietary concern not to receive any investment in India from a person resident outside India or record such investment in its books unless provided in FEMA

- **Permission for making investment by a person resident outside India**
  
  Investment made by a person resident outside India to be subject to the entry routes, investment limits and the attendant conditionalities for such investment as laid down in these regulations unless otherwise.

- **Merger or demerger or amalgamation of Indian companies**
  
  Where a Scheme of Arrangement for an Indian company has been approved by National Company Law Tribunal/ Competent Authority, the Indian company may issue non-convertible redeemable preference shares or non-convertible redeemable debentures out of its general reserves by way of distribution as bonus to the shareholders resident outside India, subject to conditions

- **Taxes and Remittance of sale proceeds**
  
  All transaction to be undertaken through banking channels in India and subject to payment of applicable taxes, duties, levies etc. in India.

Schedule 1 of the Regulation

**Permission to FPI**: FPI may purchase following debt instruments on repatriation basis subject to the terms and conditions specified by SEBI and RBI

- dated Government securities/ treasury bills (T-bills);
- non-convertible debentures/ bonds issued by an Indian company;
- commercial papers (CP) issued by an Indian company;
- units of domestic mutual funds or ETFs which invest less than or equal to 50% in equity;
- Security Receipts (SRs) issued by Asset Reconstruction Companies;
- debt instruments issued by banks, eligible for inclusion in regulatory capital;
- Credit enhanced bonds;
- Listed non-convertible/ redeemable preference shares or debentures issued in terms of Regulation 6 of these Regulations;
- Securitised debt instruments Rupee denominated bonds/ units issued by Infrastructure Debt Funds;
- Municipal Bonds

The schedule also provides for:

- permission to NRI and Overseas Citizens of India (OCI) on repatriation and non-repatriation basis,
- permission to foreign central banks or multilateral development bank for purchase of government securities.
- **Mode of payment**
• Permission for sale of instruments
• Remittance/ credit of sale / maturity proceeds.

Source: Notification Reserve Bank of India, Financial Markets Regulation Department  F.No. F. No. 1/14/EM/2015 dated 17 October 2019

❖ Government of India specified debt instruments

The Ministry of Finance (MoF), determined the following instruments as debt instruments under Foreign Exchange Management Act, 1999 (FEMA):

• Government bonds
• Corporate bonds
• All tranches of securitization structure which are not equity tranche
• Borrowings by Indian firms through loans
• DRs whose underlying securities are debt securities

Following to be considered as non-debt instruments:

• all investments in equity in incorporated entities
• capital participation in Limited Liability Partnerships (LLPs);
• all instruments of investment recognised in the Foreign Direct Investment (FDI) policy as notified from time to time;
• investment in units of Alternative Investment Fund (AIF) and Real Estate Investment Trust (REIT) and Infrastructure Investment Trusts (InvIT);
• investment in units of mutual funds and Exchange-Traded Fund (ETFs) which invest more than 50% in equity;
• the junior-most layer (i.e. equity tranche) of securitisation structure;
• acquisition, sale or dealing directly in immovable property;
• contribution to trusts;
• DRs issued against equity instruments

Any other instruments not specified above would be deemed to be debt instrument.

Source: Notification Ministry of Finance, Department of Economic Affairs, F.No. l/14/EM/2015 dated 16 October 2019

❖ Investment by FPI in Debt securities

In continuation to RBI circular no 31 dated 15 June 2018, RBI has made the below changes:

• Short-term investments by an FPI as percentage of its total investment in Central Government Securities (including Treasury Bills) or State Development Loans – limit increased from 20% to 30%.
• Short-term investments by an FPI as percentage of its total investment in corporate bonds– limit increased from 20% to 30%.
• Earlier, FPI investments in Security Receipts were exempt from the short-term investment limit. These exemptions have now been extended to FPI investments in below securities:
  ➢ Debt instruments issued by Asset Reconstruction Companies; and
  ➢ Debt instruments issued by an entity under the Corporate Insolvency Resolution Process as per the resolution plan approved by the National Company Law Tribunal under the Insolvency and Bankruptcy Code, 2016


❖ Voluntary retention route – for debt investment

❖ VRR for debt investment introduced w.e.f. 1 March 2019

Voluntary Retention Route (VRR) is a separate channel of investment in debt for FPIs. Investments through VRR to be free of macro-prudential and other regulatory norms applicable provided FPIs voluntarily commit to retain a required minimum percentage of their investments in India for a period. Participation through VRR to be entirely voluntary. VRR is effective from 1 March 2019. Key features are:
• **Eligible instruments:**
  - **VRR-Govt**: Investments in any Government Securities i.e., Central Government (CG) dated Securities, T-bills, SDLs.
  - **VRR-Corp**: Investments in any instrument listed under Schedule 5 of Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017 other than units of domestic mutual funds, G-Sec, T-bills
  - **Repo and reverse repo** transactions.

• Investment to be in addition to the General Investment Limit.

• Allocation of investment amount under VRR to be made on tap or through auctions.
  - Mode of allotment, allocation to VRR-Govt and VRR-Corp categories and minimum retention period to be announced by RBI ahead of allotment.

• FPI and its related FPIs not to be allotted investment limit greater than 50% of amount offered for each allotment by tap or auction in case demand exceeds 100 % of amount offered.

• **Minimum retention**: 3 years or as decided by RBI.

• FPIs to invest amount allocated i.e. CPS in relevant debt instruments and remain invested at all times during the period. Certain relaxations provided.

• Amounts of investment to be calculated in terms of face value of securities.

• Auction process for allocation of investment amount under VRR provided

• Management of portfolio – maintenance, exit from VRR, reporting of minor and non-minor violation aspects provided

• Relaxations from minimum residual maturity requirement, concentration limit or single/group investor-wise limits applicable to corporate bonds as specified by RBI.

• Income from VRR investments may be reinvested at the discretion of FPI. Such investments to be permitted even in excess of the CPS.

• Access to other facilities -
  - FPIs investing through VRR eligible to participate in repos for their cash management subject to conditions.
  - FPIs investing under VRR eligible to participate in any currency or interest rate derivative instrument, over the counter or exchange traded, to manage their interest rate risk/currency risk.

• Operational aspects - utilisation, repatriation, maintenance of Special Non-Resident Rupee (SNRR) Account etc. provided


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**RBI released circular on hedging of exchange rate risk by FPI under VRR.**

FPIs permitted to hedge the exposure to exchange rate on account of investments made under VRR.

Products offered for hedging to comprise of forwards, options, cost reduction structures and swaps with Rupee as one of the currencies.

**Operational Guidelines, Terms and Conditions:**

Authorised dealers (AD) may offer derivative contracts using any of the aforementioned products to eligible users under VRR or to its central treasury (of the group and being a group entity). AD to ensure

- FPI has exposure to exchange rate risk on account of VRR investments.
- Notional and tenor of the contract does not exceed the value and tenor of the exposure.
- Same exposure has not been hedged with any other AD or on the exchange.
- In cases where the value of the exposure falls below the notional of the derivative, the derivative to be suitably adjusted.

**Exception:** Such divergence has occurred due to change in market value of the exposure. The FPI may, at its discretion, continue with the derivative contract till its original maturity.

AD to allow FPIs to freely cancel / rebook derivative contracts.

AD to ensure all payables incidental to the hedge are met by the FPI out of repatriable funds and/or inward remittance through normal banking channels.

**RBI amended directions on VRR w.e.f 24 May 2019**

On the basis on the feedback received, RBI revised VRR direction with effect from 24 May 2019. The changes include:

- Introduction of a separate category – VRR combined
  
  VRR combined to mean VRR for FPI investment in instruments eligible under both VRR-Govt and VRR-Corp.
  
  Investment under this route to be capped at INR 75,000 crore or higher. The amount to be allotted amongst VRR-Govt, VRR-Corp and VRR-combined as decided by RBI.

- Removal of requirement of investing at least 25% of the combined portfolio size within one month of allotment
  
  Under the new circular, successful allottees to invest at least 75% of their CPS within three months from the date of allotment

- additional option at the end of the retention period provided to FPIs – continue to hold investments till the date of maturity or the date of sale whichever is earlier
  
  Further, FPIs can liquidate their investment partly or fully before end of the retention period subject to conditions.

- FPIs allotted investments under ‘on tap’ upto 30 April 2019 to be converted to VRR- combined.


**Relaxation provided in VRR**

RBI relaxed the VRR direction contained in circular no 34 dated 24 May 2019. The changes include:

- The investment cap is increased to from 75,000 crores to Rs. 1,50,000 crores
- FPIs are allowed to invest in Exchange Traded Funds that invest only in debt instruments.
- FPIs can, at their discretion, transfer their investments made under General Investment Limit, if any, to VRR scheme.


**Revised haircut on central G-Sec accepted as collateral**

SEBI revised minimum haircut applicable to G-Sec deposited with clearing members as collateral towards risk management in cash market. Details are as under:

<table>
<thead>
<tr>
<th>Type and Tenor of Securities</th>
<th>Haircut as per new circular</th>
<th>Haircut as per earlier framework</th>
</tr>
</thead>
<tbody>
<tr>
<td>Treasury Bills and Liquid GOI dated securities having residual maturity &lt; 3 years</td>
<td>2%</td>
<td>10%</td>
</tr>
<tr>
<td>Liquid GOI dated securities having residual maturity &gt; 3 years</td>
<td>5%</td>
<td>10%</td>
</tr>
<tr>
<td>For all other Semi-liquid and Illiquid GOI dated securities</td>
<td>10%</td>
<td>10%</td>
</tr>
</tbody>
</table>

  Source: SEBI circular SEBI/HO/MRD/DRMNP/CR/P/2019/33 dated 21 February 2019

**Amendment made to Foreign Exchange Management (Deposit) Regulations, 2016 (deposit regulations, 2016) to bring consistency in provisions.**

In order to bring consistency in statutory provisions/ regulations relating to Commercial Papers (‘CP’), the conditions provided in deposit regulations, 2016 were deleted.

As per the earlier deposit regulations, 2016, an Indian company could accept deposits by issue of CP to a non-resident Indian (‘NRI’) or a person of Indian origin (‘PIO’) or an FPI subject to below conditions:

- the issue of CP to be in compliance with the regulations issued by RBI or any government authority in regard to acceptance of deposits;
- payment for issue of CP to be received by company by inward remittance from outside India through banking channels or out of funds held in a deposit account maintained by a NRI or a PIO in accordance with the regulations made by RBI;
- amount invested in CP not to be eligible for repatriation outside India; and
- CP not to be transferable.
The above conditions above were deleted from 16 July 2019 as: the RBI Act, 1934 described CP as Money Market Instruments; Companies (Acceptance of Deposits), Rules 2014 excluded CPs from definition of deposits; and Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017 – FEMA 20(R), allowed investments in CPs issued by the Indian Companies.

Source: RBI/2019-20/44 AP (DIR series) Circular No.06 dated 16 August 2019

Framework for FPI investment in non-debt instruments

♦ RBI notified Foreign Exchange Management (Non-debt Instruments) Rules, 2019.


Key changes from provisions in FEMA 20(R) were:

- With effect from 1 April 2020, aggregate limit for FPIs to invest in Indian company to be sectoral cap in the Indian company. Previously limit for FPIs was 24% in the Indian Company.
- The Indian company can reduce the aggregate threshold limit to 24% or 49% or 74% by passing a resolution by 31 March 2020. The decreased aggregate limit can be increased by passing prescribed resolutions. However, once the aggregate limit is increased it cannot be reduced to lower threshold.
- The aggregate limit for FPI investment in an Indian Company in a FDI prohibited sector is 24%.
- In case of breach of the prescribed limit, FPI has the option to divest its holding within 5 trading days from date of settlement of trades causing such breach. In case FPI does not divest, the entire investment in such company by such FPI and its investor group would be considered as FDI.

The investment in debt instruments are covered in Foreign Exchange Management (Debt Instruments) Regulations, 2019 notified on 17 October 2019

Source: Foreign Exchange Management (Non-debt Instruments) Rules, 2019. Ministry of Finance Notification F.No. 1/14/EM/2015 date d 17 October 2019

♦ Foreign Exchange Management (Non-Debt Instruments) (Amendment) Rules, 2019

MoF made amendments to Foreign Exchange Management (Non-debt Instruments) Rules, 2019. The key changes are below:

- Earlier version of the rules permitted FPI to transfer equity instruments of an Indian company or units held by way of sale or gift to any person resident outside India. This portion was deleted in the amended rules.
- Pricing guidelines –In case of convertible equity instruments, the price or conversion formula of the instrument to be determined upfront at the time of issue of instrument. It should not be lower than fair value worked out at the time of issuance of such instruments.
- Schedule II (FPI) – In line with the erstwhile FEMA 20(R) regulations, Indian companies can increase aggregate limit of 24% upto sectoral cap, with approval of its Board of Directors/ General Body through resolutions, upto 31 Mar 2020

Source: Department of Economic Affairs, Foreign Exchange Management (Non-Debt Instruments) (Amendment) Rules, 2019 dated 5 December 2019

♦ Foreign Exchange (Mode of Payment and Reporting of Non-Debt Instruments) regulations, 2019

RBI issued notification relating to mode of payment and reporting requirements for investment in India by a person resident outside India. Instruction on mode of payment and remittance of sale proceeds:

Investment by FPI

Mode of Payment: Inward remittance from abroad through banking channels or out of funds held in a foreign currency account or SNRR account.

Balance in SNRR account not to be used for making investment in units of Investment Vehicles other than the units of domestic mutual fund.

Remittance of sale proceeds: The sale proceeds (net of taxes) of equity instruments and units of domestic mutual fund may be remitted outside India or credited to the foreign currency account or SNRR account.

The sale proceeds (net of taxes) of units of investment vehicles other than domestic mutual fund may be remitted outside India.
**Interest rate derivatives**

**RBI allows non-residents to participate in rupee interest rate derivatives market**

To regulate the financial system and in the interest of the public, RBI issued Non-resident Participation in Rupee Interest Rate Derivatives Markets (Reserve Bank) Directions, 2019 w.e.f 27 March 2019.

The key features of directions are:

- For the purpose of these directions, hedging is for reducing rupee interest rate risk
- Rupee interest rate derivative (IRDs) transactions can be undertaken on RSE, ETP and OTC markets.
- Non-resident can undertake transactions in the Rupee interest rate derivatives markets:
  - **For hedging an exposure to rupee interest rate risk**
    - Non-resident may use any permitted interest rate derivative product transacted on RSE, ETPs or OTC markets for hedging.
    - The interest rate derivative transactions should conform with applicable regulations.
    - Market-makers to ensure that transactions are being carried out for the purpose of hedging
  - **For purposes other than hedging**
    - Non-residents, other than individuals, may undertake overnight index swap transactions subject to certain arrangements and limits.
    - FPIs, collectively, may also transact in interest rate futures (IRF) up to a limit of net long position of INR 50 billion.
- Payments related may be routed through:
  - a Rupee account of the non-resident or,
  - a vostro account maintained with an AD bank in India where the non-resident does not have Rupee account in India
- Market-maker to ensure that non-resident clients:
  - are from a Financial Action Task Force (FATF) compliant country
  - comply with the KYC requirements as prescribed

**Comprehensive guidelines on rupee interest rate derivatives (Reserve Bank) Directions, 2019**

In order to achieve consistency, ease of access and to encourage environment for management of interest rate risk, RBI issued simplified comprehensive guidelines to rationalise regulations for IRDs. The key features of directions are:

- For the purpose of these directions, hedging is for reducing rupee interest rate risk
- Rupee interest rate derivative transactions can be undertaken on RSE, ETP, OTC markets.
- **Directions for IRD carried on RSE**
  - RSE permitted to offer any IRF or interest rate options (IRO) products, including swaptions.
  - The product design, eligible participants and other details of IRD may be decided by RSE
  - RSE to obtain prior approval of RBI before introducing any new IRD contract or before carrying out modifications to an existing contract.
- **Directions for IRD carried in OTC for hedging an exposure to rupee interest rate risk**
  - Scheduled Commercial Banks, Primary Dealers and All-India Financial Institutions (FIs) are eligible to act as market-makers for IRD products in OTC markets.
Market-makers may offer the following products to users:-

- Forward Rate Agreement,
- Interest Rate Swap,
- European Interest Rate Options
- swaptions and structured derivative products (permitted for non-retail users)

Market makers to classify users either as a retail user or as a non-retail user.

Market makers to ensure that transactions undertaken by retail users are for the purpose of hedging an underlying interest rate risk.

Floating interest rate or price or index used in IRDs in the OTC market to be a benchmark published by Financial Benchmarks India Pvt. Ltd / authorised benchmark administrator.

IRD transactions to be settled bilaterally or through any approved clearing arrangement

Settlement basis and other market conventions to be specified by FIMMDA, in consultation with market participants.

- **Conditions applicable to IRDs on both exchanges and in the OTC market**
  
  Market makers in OTC markets to comply with the ‘suitability and appropriateness’ requirements contained in circular on Comprehensive Guidelines on Derivatives issued by RBI.

  RSE to ensure that participants are adequately made aware of the risks associated with the derivative instrument.

  Accounting and capital requirement for IRDs to be as specified by the respective regulators of participants or as per the applicable accounting standards prescribed

Pursuant to RBI publication of draft directions in April 2019 for public comments, RBI released the final directions with effect from 26 June 2019.

In addition to the existing products for retail users, RBI has included interest rate caps, floors, collars and reserve collars.

**Position Limit in Interest Rate Derivative**

SEBI revised the position limit for interest rate derivatives falling in the 8-11 years maturity bucket.

<table>
<thead>
<tr>
<th>Category</th>
<th>Position limits for 8-11 year bucket</th>
<th>Position limits each for 4-8 and 11-15 years bucket</th>
</tr>
</thead>
<tbody>
<tr>
<td>Institutions in Category I and II FPIs (other than individuals, family offices and companies), other entities</td>
<td>10% of Open Interest or INR12 billion whichever is higher</td>
<td>10% of Open Interest or INR 6 billion whichever is higher</td>
</tr>
<tr>
<td>Non-institutions in Category II FPIs (i.e. individuals, family offices and companies), other entities</td>
<td>3% of Open Interest or INR 4 billion whichever is higher</td>
<td>3% of Open Interest or INR 2 billion whichever is higher</td>
</tr>
</tbody>
</table>

**Units of REITS and InvITs**

**Guidelines for allotment and trading lot size for publicly traded REITs, InvITs**

SEBI issued guidelines for determination of allotment and trading lot size for REITs and InvITs. The guidelines are as under:

**For allotment of initial offer:**

- The value of each allotment lot not to be less than INR 1 lakh for InvITs and INR 50,000 for REITs, where such lot shall consist of 100 units.
- Allotment to any investor shall be made in multiples of a lot

**For follow-on offer:**

- Minimum allotment to be of such number of lots, whose value is not less than INR 1 lakh for InvITs and INR 50,000 for REITs, where each lot shall consist of such number of units as in its trading lot.
• Allotment to any investor shall be made in the multiples of a lot.

Stock exchange, in consultation with publicly offered InvITs/REITs to determine number of units in the trading lot for such REITs/InvITs, within a period of 6 months from the date of this circular.

Other changes include disclosure requirements by InvITs such as: debt equity ratio, net worth etc.

Source: SEBI circular SEBI/HO/DDHS/DDHS/CIR/P/2019/59 dated 23 April 2019

❖ Preferential issue of units and institutional placement of units by a listed REIT and InvIT

SEBI issued guidelines on preferential issue of units and institutional placement of units by a listed REIT/ InvITs. Some of the key aspects are as under:

• Issuer to comply with listing and disclosure obligations as applicable.
• Issuer to disclose objective of the issue, related-party transactions, valuation, financial details, review of credit rating etc.
• Institutional Placement to mean preferential issue of units by a listed InvIT/ REIT only to Institutional Investors, as defined in InvIT/ REIT Regulations.
• The units to be allotted in dematerialized form and listed on stock exchange
• Consideration for units to be fully paid.
• Allottee can sell the units allotted through institutional investor prior to one year from date of allotment on recognised stock exchange
• Units to be listed within 7 days from date of allotment

Source: SEBI circulars SEBI/HO/DDHS/DDHS/CIR/P/2019/142 and SEBI/HO/DDHS/DDHS/CIR/P/2019/143 dated 27 November 2019

Other relevant changes

❖ RBI provides responses to FAQ for IFSC

IFSC units and other participants/ investor raised various queries to RBI. Few responses are provided:

• Indian banks and foreign banks permitted to set up IFSC Banking Unit, subject to prior permission and minimum capital requirements.
• IBUs can open foreign currency accounts of units operating in IFSC and of non-resident institutional investors for the purpose of trading and investment activities.
• A financial institution or a branch of a financial institution set up in IFSC and permitted/ recognized as such by GOI/ regulatory authority to be treated as 'Person resident outside India'
• A person resident in India can invest in financial institution set up in IFSC. The investment is to be in accordance with Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004. Resident Indians not permitted to use Liberalised Remittance Scheme remittances for investments in IFSC.
• Financial institutions in IFSC eligible to open and maintain SNRR account with a bank in India (outside IFSC)
• Entities in IBU to be guided by RBI Mater Direction for KYC. IBU can rely on customer due diligence done by a third party.
• Dealings by financial institutions to be determined by regulatory authority.
• A bank account in IFSC to be treated as bank account outside India.
• Investing FPIs holding foreign currency account in India can transfer funds from the said account to any bank account in IFSC.
• Persons not eligible to open accounts but allowed to transact in IFSC have to transfer funds from their bank account outside IFSC to bank account of the beneficiary.
• Individuals not allowed to open accounts in IFSC

Source: GIFT SEZ Limited FAQ for IFSC dated 1 March 2019
Introduction of Rupee derivatives at International Financial Services Centre (IFSC)

RBI issued directions permitting Rupee derivatives (futures and options) with settlement in foreign currency to be traded in IFSC. The key features are:

- Currency derivatives (F&O) in any currency pair involving the Rupee or otherwise are permitted on recognised stock exchanges set up in IFSCs
- Contracts (F&O) in the Rupee to be settled in a currency other than the Indian Rupee.
- The settlement price for currency future or option involving rupee to be Financial Benchmarks India Private Limited reference rate on the last trading day or expiry date of the contract respectively.
- Size, maturity and other specification of the derivative contract to be decided by stock exchange in consultation with SEBI.
- Premium for currency option contract to be quoted in currency other than INR.
- Person resident outside India may undertake these derivative contracts.


SEBI specifies categories of FPI to whom Asset Management Company (AMC) can provide services

AMC can provide management and advisory services as provided in SEBI (Mutual Fund) Regulations, 1996 to the below categories of FPIs

- Government and government related investors
- Appropriately regulated entities such as pension funds, insurance or reinsurance entities, banks and mutual funds.
- Appropriately regulated FPI wherein above-mentioned entities both or one of them hold more than 50% of shares/units.

In case where agreement was entered into by the AMCs on or before 16 December 2019, the AMC may provide management and advisory services to FPIs, not falling under above categories, for a period as mentioned in the agreement, or one year from the date of this circular, whichever is earlier.

Above categories of FPI are exempt from appointing separate Fund Manager for each fund managed by AMC.

Source: SEBI circular SEBI/HO/IMD/DF2/CIR/P/2019/155 dated 16 December 2019

Additional criteria for movement of stock derivative to physical settlement

SEBI added criteria to existing schedule of stock derivative moving to physical settlement. If any of the physical settlement criteria are satisfied, the derivative to be moved to physical settlement from new expiry cycle:

- Stocks with 10% or more intra-day movement on 10 or more occasions in last 6 months, or
- Stocks with 10% or more intra-day movement on 3 or more occasions in last 1 month, or
- Stocks with 25% or more intra-day movement on 1 or more occasions in last 1 month, or
- Maximum daily volatility of the stock (estimated for margining purpose) is more than 10% either in equity or equity derivatives segment in the last 1 month.

Source: SEBI circular SEBI/HO/MRD/DOP1/CIR/P/2019/28 dated 8 February 2019

Shares with Differential Voting Rights (DVRs)

SEBI constituted group submitted a report on proposal of introduction of dual-class shares in Indian companies inviting public comments by 20 April 2019. SEBI Board meeting in Mumbai on 27 June 2019, discussed and approved frame work for issuance of DVRs.

Key proposals were:

Eligibility - issuance of superior voting rights shares (SR)

- Issuer company is a technology intensive company
- SR shareholder to be part of promoter group whose collective net worth does not exceed INR 500 crores.
- SR have been issued only to promoters who hold an executive position in the company.
- Issue of SR authorised by special resolution passed at a general meeting of the shareholders.
2. Tax Updates

Union Budget 2019 and increase in surcharge

- **Finance Budget 2019**

The Honorable Finance Minister of India, Ms. Nirmala Sitharaman presented the Union Budget 2019 before the Parliament on 5 July 2019. Key Budget Highlights relevant to FPIs are as under:

**Regulatory**

- To permit FPIs to subscribe to listed debt securities of ReITs, InvITs
- To permit FPI to transfer debt securities issued by Infrastructure Debt Fund- Non-Banking Finance Companies to any domestic investor within specified lock-in period
- To increase statutory limit of FPI investment in a company from 24% to sectoral foreign investment limit with an option given to the concerned corporate to limit it to lower threshold
- To merge the NRI- Portfolio Investment Scheme Route with the FPI Route
- To rationalize and streamline existing KYC norms for FPIs
- To examine suggestions of further opening up of FDI in aviation, media (Animation, Visual Effects, Gaming and Comics) and insurance sectors in consultation with all stakeholders.
- FDI upto 100% to be allowed for insurance intermediaries such as brokers, corporate agents, and third party administrators.

**Taxation**

- Increase in surcharge rates for individual, Hindu undivided family, association of persons, body of individuals or artificial juridical person.
- Surcharge rate to be increased from 15% to 25% where total income exceeds INR 20 million and from 15% to 35% where total income exceeds INR 50 million.
- Separate filing of Form No. 30 is not required for claiming income tax refund
- Exemption of interest income in the hands of non-resident arising from borrowings by way of issue of Rupee Denominated Bonds (‘RDB’) earned during the period 17 Sep 2018 to 31 March 2019
- Concessional rate of 15% of STCG tax extended to certain equity-oriented fund of funds.
- Relaxation in eligibility conditions in relation to corpus of the investment fund and remuneration paid to fund manager for offshore funds
- Persons who deposit an amount or aggregate amounts exceeding INR 10 million in one or more current account with a bank during the financial year mandatorily required to file return of income.
- Tax on income distributed to shareholder in case of listed companies u/s 115QA of the Act
- Widen scope- Statement of Financial Transactions
- Penalty for under-reporting, misreporting income
- Rationalization of provision relating to recovery of tax in pursuance of agreements entered into with foreign countries.

Source: Finance (No.2) Bill 2019 dated 5 July 2019
Government withdraws enhanced surcharge in respect of tax payable on transfer of certain assets

On 5th July 2019, the Government of India (GOI) vide Finance (No.2) Bill, 2019 proposed to increase surcharge rates for individual, Hindu undivided family, association of persons, body of individuals or artificial juridical person. The Finance (No.2) Bill 2019 received assent of the President of India on 1 August 2019 and this provision came into effect from 1 April 2019.

Based on the feedback received from various stakeholders, Central Board of Direct Taxes (CBDT) vide its press release decided to withdraw enhanced surcharge on tax payable. The withdrawal of enhanced surcharge was to apply on transfer of equity shares of a company, units of equity-oriented fund, unit of a business trust covered under ambit of section 111A or 112A of the Income-tax Act, 1961 (the Act) (for all types of investors) and gains arising on transfer of derivative transactions (futures and options) liable to rate of tax u/s 115AD of the Act (for FPIs only).

On 20 September 2019, the President of India promulgated an ordinance to withdraw the enhanced surcharge w.e.f. from 1 April 2019 to give effect to the above. The withdrawal of enhanced surcharge was extended to tax on sale of any security by FPIs.

The Taxation Laws (Amendment) Bill, 2019, was introduced to replace the Taxation Laws (Amendment) Ordinance, 2019 which, received Presidential assent on 11 December 2019 and the same was published in the Official Gazette of India on 12 December 2019 thereby becoming a law.


Tax on distributed income and other issues

Tax on income distributed to shareholder in case of listed companies

The Finance (No.2) Bill, 2019 extended the scope of section 115QA of the Act to domestic listed companies whereby companies are liable to pay additional income-tax at the rate of 20% (excluding surcharge and health and education cess) on the distributed income on account of buy-back of shares. The income would be exempt from tax in the hands of the shareholders w.e.f 5 July 2019.

The President of India promulgated an ordinance providing exemption from tax on distributed income to Indian companies in case where public announcement for buy-back was made before 5 July 2019. Subsequently, the Taxation Laws (Amendment) Bill, 2019, which was introduced to replace the Taxation Laws (Amendment) Ordinance, 2019, received Presidential assent on 11 December 2019 and the same was published in the official Gazette of India on 12 December 2019.


Clarification on perceived differential taxation of FPIs and domestic investors

CBDT vide its press clarified that differential regime between domestic investors (including AIF category III) and FPIs existed even prior to the 2019 budget and was not creation of the Finance (No 2) Act, 2019 or announcement made by the Finance Minister on 23 August 2019.

Section 115AD read with section 2(14) of the Act contained special provisions for FPIs for taxation of income from derivatives. Income of FPIs from derivatives is treated as capital gains liable for special rate of tax.

However, income arising from derivatives for the domestic investors including AIF (category-III) as well as for foreign investors who are not FPIs, have been treated as business income and not as capital gains, and taxed at applicable normal income tax rates.

Source: CBDT Press Release dated 28 August 2019

Stamp duty

Amendment to Indian Stamp Duty Act, 1899 for rationalization of stamp duty

Finance Bill of 2019 provided for reform measures in stamp duty regime on financial securities transactions. Objective was to facilitate ease of doing business, bring uniformity, build pan-India securities market, expected to lead to zero tax evasion. Salient features of the amendment are as follows:

- Collection of stamp duty by states to be at one place by one agency.
• Each security to be charged with a duty specified in the Stamp Duty Act. Government securities and instruments based on government securities excluded from stamp duty.

• Rates to apply only on one side of the transaction i.e. either by buyer or seller.

• Stamp duty to normally apply on transaction value. Exceptions: - on swaps - the first leg of cash flow, on option - its premium, on repo on corporate bond - interest paid by borrower to be considered.

• For exchange based secondary market transactions in securities, stock exchange to collect duty. For off market transaction and initial issue of securities in demat form, depositories to collect the duty.

• State of domicile of the buying client or of the broking house/ depository participant of the buying client to be taken as the basis for remitting duty to respective states.

• Tax arbitrage avoided by providing same rate of stamp duty for issue or re-issue or sale or transfer of securities happening outside stock exchange and depositories.


❖ Indian Stamp (Collection Taxation Laws (Amendment) Bill, 2019 received Presidential assent

On 10 December 2019, the CG notified that the amended stamp duty regime will be effective from 9 January 2020. Alongside this, the rules prescribing the procedural aspects regarding collection and payment mechanism of stamp duty were notified with effect from 9 January 2020. With this, the new stamp duty regime is set to kick off from 9 January 2020. The rules prescribe procedural aspects regarding collection, transfer of stamp duty


❖ Applicability of amended stamp duty regime deferred

On 10 December 2019, CG had notified that the amended stamp duty regime to be effective from 9 January 2020. Further, the rules prescribing the procedural aspects regarding collection and payment mechanism of stamp duty were notified to be effective from 9 January 2020.

However, the CG has deferred the applicability of amended stamp duty regime and the rules prescribed thereunder from 9 January 2020 to 1 April 2020.


❖ Progress on new direct tax legislation

❖ Task Force constituted for drafting direct tax legislation.

A Task Force was constituted in November 2017 to submit report on draft of an appropriate direct tax legislation within 6 months from constitution. While drafting, the task force to keep in view:

• Direct tax system prevalent in various countries

• International best practices

• Economic needs of the country and

• Any other matter connected thereto

The term was extended to 28 February 2019, later extended to 31 May 2019 and thereafter the term of the task force was upto 31 July 2019.

Further, GOI broadened the terms of reference to include

• Faceless and anonymised verification/ scrutiny/ assessment

• Mechanism for system based cross verification of the financial transactions

• Reduction in litigation and expeditious disposal or appeals before the Commissioner of Income Tax (Appeals) [CIT(A)], High Court (HC) and Supreme Court (SC).

• Reduction of compliance burden by simplification of procedures

• Sharing of information between Goods and Service Tax, Customs, CBDT & Financial Intelligence Unit.

Term of Task Force constituted for drafting new direct tax law extended

The term of the Task Force was extended to 31 July 2019. The Task Force was required to submit its report by 16 August 2019.

The task force submitted the report on 19 August 2019 to overhaul the six-decades-old Income Tax Act. However, the Ministry kept mum on the recommendations made by the task force. Also, it is yet to place the report in the public domain for further consultation.


Filing of income tax returns for AY 2019-20

CBDT extends due date for filing of income tax returns for AY 2019-20

For categories of tax payers who were liable to file return of income (and tax audit report, as applicable) by 31 July 2019 or 30 September 2019, the due date was extended to 31 August 2019 and 31 October 2019 respectively.


CBDT issues clarification in respect of filling up of the ITR forms for AY 2019-20

After ITR forms were notified, various queries were raised by stakeholders. In order to address such queries, CBDT issued clarification. Few of the relevant clarifications are:

- Where the assessee holds equity shares of unlisted company at any time during the year, Permanent Account Number (PAN) of the company may be furnished if available or default value may be entered “NNNNNN00000N” where PAN cannot be obtained.
- The tools for computation of long term capital gain (LTCG) u/s 112A and 115AD were provided in utility for the convenience of taxpayers wherein ISIN details and scrip wise computation is provided. These are optional tools. Alternatively, the taxpayers can compute the aggregate LTCG/ Long term capital loss (LTCL) manually and input the values directly in the ITR.
- The break-up of receipts and payments in foreign currency under schedule FR of ITR-6 is required to be reported only in respect of business operations in India.

Source: CBDT Circular No. 18 of 2019 dated 8 August 2019

Fund management activity in India

Clarification regarding definition of Fund Manager u/s 9A of the Act

As per section 9A of the Act, fund management activity of an eligible investment fund, carried out through an eligible fund manager acting on behalf of such fund does not constitute business connection in India of the said fund subject to certain conditions.

In this regard, CBDT, in consultation with SEBI, issued circular clarifying that definition of “Fund Manager” u/s 9A(4)(b) of the Act includes SEBI registered AMC. AMC is engaged in the activity of fund management of mutual funds and hence it is in substance a fund manager.


CBDT seeks comments on the draft notification on framing of rules with respect to Fund Manager Regime u/s 9A of the Act

Section 9A of the Act provides for a special taxation regime in respect of certain offshore funds in context of their fund managers located in India. In case of an eligible investment fund, the fund management activity carried out through an eligible fund manager acting on behalf of such fund should not constitute business connection in India subject to conditions mentioned in Section 9A(3). One of the conditions provide that the remuneration paid by the fund to an eligible fund manager in respect of fund management activity undertaken by him on its behalf is not less than the arm’s length price of the said activity.

The Finance (No 2) Act, 2019 amended the said provision so as to provide that the remuneration paid should not be less than the amount calculated in such manner as may be prescribed.

In this regard, CBDT issued notification providing draft rules and various criteria for manner of calculation of the amount of remuneration to be paid by the fund to a fund manager. Comments were to be submitted by 19 December 2019.

Source: CBDT notification F. No 142/15/2015-TPL dated 5 December 2019
Approval of MLI

The GOI issued a press release stating that Union Cabinet has approved the ratification of Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI). MLI seeks to implement tax treaty related measures to prevent Base Erosion and Profit Shifting (BEPS).

The Convention will modify India’s treaties in order to curb revenue loss through treaty abuse and BEPS strategies by ensuring that profits are taxed where substantive economic activities generating the profits are carried out and where value is created.

India deposited its instrument of ratification for MLI with list of reservations and notifications on 25 June 2019.

Source: PIB release Cabinet dated 12 June 2019 and 25 June 2019

Ratification by India of the MLI

India had deposited its instrument for ratification for MLI on 25 June 2019. Depending on the position taken under MLI by a country, India’s DTAA with it to get modified in the following prominent ways:

- The minimum standard under BEPS Action 6 to tackle treaty abuse, i.e., insertion of new Preamble and the Principal Purposes Test (PPT) in the DTAA to be achieved.
- The minimum standard under BEPS Action 14 relating to the mutual agreement procedure to be implemented.
- Artificial avoidance of Permanent Establishment (PE) status through commissionaire arrangements and similar strategies to be prevented. Avoidance of PE formation through specific activity exemptions and splitting up of contracts to also be prevented.
- Avenues leading to avoidance of capital gains tax from alienation of shares/interests deriving value principally from immovable property to be plugged.
- Certain dividend transfer transactions that are intended to lower withholding taxes payable on dividends artificially to be prevented.

The date of entry into force of the MLI is 1 October 2019. In respect of the 22 treaty partners of India who have deposited the Instrument of Ratification on or before 30th June 2019, entry into effect for India under MLI with respect to the DTAA to be from financial year 2020-21 onwards. For the remaining CTAs, effect of MLI will take place as and when the countries ratify the MLI.

Source: CBDT Press Release dated 2 July 2019

CBDT Guidelines and Directions – assessments, appeals, refunds etc.

E-assessment Scheme, 2019

CBDT notified E-assessment Scheme, 2019 (the Scheme) u/s 143(3A) of the Act. For the purpose of the Scheme the government may set-up E-assessment centres (National e-assessment centre, Regional e-assessment centres, assessment units, verification units, technical units, review units) and specify their respective jurisdiction.

All communication among the assessment unit, review unit, verification unit or technical unit or with the taxpayer or any other person with respect to the information or documents or evidence or any other details, as may be necessary for the purposes of making an assessment under the Scheme is to be through the National e-assessment centre.

The Scheme also prescribes the procedure for E-assessment and penalty for non-compliance of any notice, direction or order issued under the Scheme by the taxpayer or any other person.


CBDT issues directions for conduct of assessment proceedings through e-proceeding facility

Assessment proceedings to be conducted electronically during financial year 2019-20. In cases listed below, it is not mandatory that assessment be through e-proceeding.

- Assessment framed u/s 153A, 153C, 144 of the Act for search.
- Set-aside assessments
• Assessment framed in non-PAN cases
• ITR filed in paper mode and assessee does not yet have e-filing account
• Cases of stations connected through Very Small Aperture Terminal or with limited capacity bandwidth.
• Cases of extraordinary circumstances- complexities, administrative difficulties

Personal hearing may take place in the following cases where e-proceedings are carried out:
• Books of accounts to be examined
• Assessing officer (AO) invokes section 131 of the Act for production of evidence
• Examination of witness required
• Show cause notice contemplating adverse view is issued by AO and assessee request for personal hearing.

Source: CBDT circular No. 27/ 2019 dated 26 September 2019

❖ Guidelines for manual selection of return for complete scrutiny in F.Y. 2019-20

CBDT provided following parameters for manual selection of cases:
• Where addition was made in earlier assessments on a recurring issue of law or fact:
  ➢ In case where the addition exceeds **INR 2.5 million** in metro cities and **INR 1 million** in other cities and or exceeding **INR 100 million** in transfer pricing cases.
  ➢ Where such addition
    o is final and no further appeal was filed
    o was confirmed at any stage of appellate process in favour of revenue and assessee has not filed further appeal
    o was confirmed at any stage of appeal in favour of revenue even if appeal of assessee is pending
• Survey u/s 133A
• Assessment in search and seizure cases
• Where certain registration/ approval is not granted/ earlier granted under the Act has been withdrawn but the assessee has found to be claiming tax exemption/ deduction.
• Information relating to specific tax evasion for relevant year shared by govt. authorities.
• Cases selected for scrutiny through Computer Aided Selection of Cases (CASS) but not verified within time provided - to be reopened u/s 148
• Issues arising from information provided by law enforcement agencies can be examined for cases selected for limited scrutiny.

Source: CBDT circular F. No 225/169/2019/ITA-II dated 5 September 2019

❖ Reconstitution of CASS committee

CBDT issued an Office Memorandum reconstituting CASS Committee. The Terms of Reference for the CASS Committee are as follows:
• Analysis of suggestions received from field authorities.
• Recommendation of modification or removal of existing rules.
• Recommendation of introduction of new rules.
• Recommending changes in Income-tax returns, Income-tax forms, third party information, etc., to enable effective scrutiny selection.
• Formulation of rules and selection of cases from Non-filers Monitoring System.

Source: Office Memorandum F. No DGIT(RA)aDG-1/CASS/2019-20 dated 3 January 2020
Comments sought on draft Rule 29BA & Form 15E

CBDT issued an Office Memorandum proposing an amendment in the Income-tax Rules 1962, to insert a new Rule 29BA and Form 15E, to give effect to the amendments in Section 195 of the Act.

In order to have a systematic and standard process for making an application by the deductor u/s 195 of the Act and to reduce human interface, CBDT released draft form 15E and manner of filing of application to the AO to determine the appropriate proportion of such sum so chargeable and upon determination tax to be deducted.

Comments were sought within 15 days of publication of the Memorandum i.e. by 15 January 2020.

Instructions issued for filing application for lower/nil tax deduction certificate

In view of the time being taken to process the online request for lower/nil deduction tax certificate and to facilitate applicants to get certificates w.e.f 1 April of the financial year (FY), the applicants can apply for lower/nil deduction certificate from 28 February of immediately preceding FY for the next FY (i.e. 28 February for FY 2020-21).

Further, as the time required for obtaining relevant data from various sources and subsequent processing of online requests for certificate, no request for issue of certificates for a FY to be accepted after 15th of March of the said FY (i.e. 15 March for FY 2019-20).

The above to also apply to cases for tax collection at source.

Enhancement of monetary limits for filing of appeals by tax department

As a step towards management of litigation, CBDT enhanced the monetary limits (in terms of tax effect) in filing of appeals in income-tax cases

<table>
<thead>
<tr>
<th>Appeals/ SLPs in Income-tax matters</th>
<th>New monetary limit (in INR)</th>
<th>Earlier monetary limit (in INR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Before Appellate Tribunal</td>
<td>50,00,000</td>
<td>20,00,000</td>
</tr>
<tr>
<td>Before High Court</td>
<td>1,00,00,000</td>
<td>50,00,000</td>
</tr>
<tr>
<td>Before Supreme Court</td>
<td>2,00,00,000</td>
<td>1,00,00,000</td>
</tr>
</tbody>
</table>

Tax effect for each assessment year to be calculated separately for each assessee.

On 20 August 2019, CBDT clarified that the revised monetary limits are applicable to all pending SLP/appeals/ cross objections/ references. All such pending appeals within the revised limits to be withdrawn on or before 31 October 2019.

Processing of tax returns with refund claims beyond prescribed time limit in case of no scrutiny

CBDT relaxed time frame prescribed under the Act and directed that all validly filed returns up to AY 2017-18 with refund claims which could not be processed, can be processed with prior approval from Pr.CCIT/CCIT by 31 Dec 2019. This is because due to technical reasons, subject returns filed u/s 139 or 142 could not be processed.

The extension is not available in case of:

- Returns under scrutiny assessment
- Returns where either demand is shown payable or is likely to arise after processing
- Returns remain unprocessed for reasons attributable to assessee

Constitution of committees to examine suggestions and issues on tax litigation management and International good practices

CBDT constituted a committee to examine how international good practices on tax disputes and diagnostic tool could be used for tax litigation management. CBDT constituted another committee to examine suggestions/ issues on litigation management emerging. The terms of the second committee were:
• To examine suggestions/ issues on litigation management arising out of Judicial Conference and to report on solutions and way forward

• To examine cases where Income Tax Appellate Tribunal (ITAT) passed perverse / irregular orders or where the submissions of DRs have not been recorded by ITAT to be appropriately taken up with the president, ITAT/Ministry of Law

• To examine feasibility of creation of separate bench of ITAT for international tax at places where the pendency of such cases is high/above threshold limit

• To examine suggestion of reviving of institution of junior department representative in view of shortage of department representative in ITAT

The committees to submit reports by 7 March 2019.

Source: CBDT Office Memorandum F. No. 279/Misc./M-120/2018-(ITJ), CBDT vide Office Memorandum F. No. 279/Misc./M-120/2018-(ITJ), dated 8 February 2019

❖ Guidelines for Principal Chief Commissioner of Income Tax for representation of cases before CIT(A) and formation of ‘Regional and National Talent Pool’

CBDT issued notice providing guidelines to be considered while representing before CIT(A). CBDT released Central Action Plan for 2018-19 wherein litigation management was one of the key focus areas. It stated that each AO is to identify top 20 cases of quality assessments and make proper representation in these cases before CIT(A), either personally or by filing written submissions.

Further, CBDT directed Pr.CCIT/CCITs to form a ‘Regional Talent Pool’ and National Talent Pool’ whereby it directed Pr.CIT/ CIT to identify officers having expertise/ domain knowledge in specific trade/sector/section of the Act to represent high stake cases at different levels of appeal and also for rendering all possible assistance and briefing of Counsels in such cases.

Source: CBDT F. No. 279/Misc./M-124/2018-ITJ dated 14 February 2019

❖ Exemption from filing return of income by certain class of person investing into IFSC

CG exempted non-resident tax payers from furnishing return of income u/s 139 from AY 2019-20 onwards where such persons have any income from any investment in an investment fund set up in an IFSC located in India subject to below conditions:

• TDS has been withheld on income and remitted to the CG by the investment fund at the rate provided in section 194LBB of the Act; and

• there is no other income during the year for which the persons would liable to file the tax-return.


Case laws - key decisions

❖ Beneficiary constituent’s residential status and taxability is relevant while determining tax treaty eligibility of a ‘fiscally transparent entity’

The assessee was a trustee of a fiscally transparent Dutch fund. All the participants of the fund are tax residents of Netherlands. During the year, the assessee, earned short term capital gains (STCG) on account of sale of shares in India and claimed relief under Article 13 (Capital Gains) of India-Netherlands Double Tax Avoidance Agreement (DTAA).

During assessment, the AO denied the claim of tax treaty stating that as the assessee is not a tax resident entity of Netherlands, the benefit of Article 13 will not be available.

ITAT rejected Revenue’s stand that since the fund is not a tax resident of Netherlands, treaty benefits should be denied and held that assessee’s role is that of a custodian of investments and profits accruing to the assessee are not its own, but of the assessee’s constituents.

It held that when an assessee acts as a representative assessee of a tax transparent entity, status of beneficiaries or constituents of tax transparent entities is relevant for the purpose of determining treaty protection.

Source: ING Bewaar Maatschappij I BV - As trustees of ING Emerging Markets Equity Fund vs DCIT ITA No. 7119/Mum/2014 (Bombay Tribunal) dated 27 November 2019

❖ Exemption u/s 10(38) no bar to allow carry forward of LTCL on listed shares

Assessee had claimed LTCG exemption u/s 10(38) of the Act on sale of listed shares and carried forward LTCL on sale of such shares for set-off.

The AO denied carry forward of LTCL stating that since LTCG is eligible for exemption, LTCL should be ignored and the term ‘income’ includes loss. CIT(A) confirmed AO’s decision.

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On appeal, ITAT directed the AO to permit assessee to carry forward LTCL.

ITAT clarified that judicial concept of term ‘income’ includes loss can be applied when the entire source of such income falls within the charging provisions of the Act. In a case where the source of income is otherwise chargeable to tax but only a specific specie of income derived from such source is granted exemption, then in such case the proposition that the term ‘income’ includes loss will not be applicable.

Source: M/s United Investments vs. ACIT Kol ITAT ITA No. 511/Kol/2017 dtd 1 July 2019

♦ Capital gains on sale of shares of Indian real estate companies not taxable in India as per India-Spain DTAA

A Spanish FPI claimed tax treaty benefits under Article 14(6) of India-Spain DTAA, residuary clause for taxation of capital gain as per which such capital gains, are taxed in the country where the alienator is resident. Two issues emerged:

Issue 1: Capital gains arising to assessee on sale of shares of Indian real estate companies were not taxable in India under Article 14(6) of the India-Spain DTAA.

ITAT rejected Revenue’s stand that the gains were covered by Article 14(4) and hence taxable in source jurisdiction i.e. India. The said Indian companies were not in business of holding real estate assets as investments. There was no indirect transfer of ownership of immovable properties by transfer of such shares. ITAT held that just because a company is dealing in real estate development does not imply, or even suggest, that over 50% of its aggregate assets consist of immovable properties.

Issue 2: Gains on foreign exchange transactions.

ITAT rejected Revenue’s contention that the receipt would be in the nature of income from other source and taxable in India as per Article 23 of the DTAA. ITAT held that once forward exchange contracts were entered into, with or without the regulatory approval, in the course of business, such contracts could either be in the revenue field or in capital field. These two paths are mutually exclusive, and there would not be a third path. The classification for business profits or capital gains depends on which conditions are satisfied. Further, the income is not in nature of other sources. Article 23 does not apply to items of income which can be classified under Articles 6 to 22 of the said DTAA.

In view of the above, ITAT dismissed the appeal.

Source: JCIT vs Merrill Lynch Capital Market Espana SA SV ITA No. 6108/Mum/2018 (Mumbai ITAT) dated 11 October 2019

♦ HC accepts assessee computation of cost of acquisition with respect to equity shares received on conversion of FCCB.

In 2006, assessee subscribed to Zero-Coupon FCCB in an Indian company. The assessee had converted FCCB into the underlying shares. The assessee sold the underlying equity shares acquired on conversion of the FCCBs and reported STCG.

The department rejected assessee’s stand that in view of sec. 49(2A), the cost of acquisition of the shares was to be determined with reference to the acquisition of the FCCBs.

On filing of writ, HC accepted assessee’s STCG working considering the cost of acquisition of the shares to be the closing price of the shares of the company on the NSE on the date of conversion and accepted assessee’s reliance on the FCCB Scheme notified by Govt.

Source: Kingfisher Capital CLO Ltd. vs CIT Bombay High Court Writ Petition No 19262 of 2018 dated 27 March 2019

♦ Claim of carry-forward of losses by investment series (funds) rejected

Pursuant to reorganization, petitioner was converted from a trust into a LLC in accordance with US regulations. Since assessee continued to be same person, both in its earlier status as a trust and as LLC, it had claimed carry forward of losses incurred by its constituents / series (funds), which was denied by AAR.

HC accepted that trust and LLC, continued to be the same person. Also, HC accepted that gain / loss earned by it in its earlier avatar would in law, not be denied only because of change in status from Trust to LLC. However, HC observed that petitioner is not an assessee under the Act as the return of income was not filed by it, but by its three series (funds) who were individually assigned PAN. HC accepted Revenue’s stand that having not filed return of income, petitioner was not entitled to claim benefit of carry forward of losses.

HC clarified that that the decision will not impact the case of the three series (funds) to claim the benefit of carrying forward losses u/s. 74 of the Act, if they are otherwise entitled to it in law.

Source: Aberdeen Institutional Commingled Funds LLC v. AAR (Bom HC) Writ Petition dated 8 March 2019
Change in address to be intimated to AO and PAN records to be updated

Assessee filed ROI mentioning a new address. AO initiated scrutiny assessment proceedings and sent notices at the address mentioned in PAN database. The assessee challenged the notice issued u/s 143(2) and 142(1) of the Act on the ground that the said notices were not served upon the assessee.

On appeal, SC ruled in favour of Revenue and held that mere mentioning the new address in the ROI without specifically intimating change of address to AO and without getting the PAN database updated, is not enough or sufficient to discharge responsibility for observing proper procedural steps.

In absence of specific intimation, the AO is justified in sending the notice at the available address mentioned in the PAN database. The case was remanded to CIT(A) to decide on merits.

Source: Pr. CIT vs M/s Iven Interactive Limited Civil Appeal No.8132 OF 2019 dated 18 October 2019

Capital gains on sale of shares under group re-organisation not taxable under the erstwhile Article 13(4) India-Mauritius tax treaty

A Mauritian based company sold its entire holding in wholly owned Indian subsidiary to Singaporean affiliate, pursuant to worldwide group restructuring at fair market price prevailing at that time. Applicant filed for advance ruling to decide taxability of the transaction under India Mauritius DTAA. The Revenue contended that the transaction was a colorable transaction to avoid taxes and that the Applicant was not the beneficial owner.

Advance Ruling Authority (AAR) stated that even though purchase in shares of Indian company was made from funds received from the Applicant’s parent entity and sales proceeds would ultimately go back to the parent, Applicant is still a separate entity. It distinguished it from other case wherein the equity shares of Indian company were issued in name of Mauritian entity but all the rights in respect of said equity shares were vested with the USA company.

AAR considered the period of holding of investment and regulatory approvals taken, reasons for transfer of shares, consideration received by Applicant and the protocol amending DTAA and held that capital gain arose in hands of Applicant and Applicant was eligible for availing treaty benefits under Article 13 of DTAA.

Source: Becton Dickinson (Mauritius) Ltd (AAR NCR Bench) AAR No. 1306 of 2012 dated 11 September 2019

STCG arising to Non Resident on sale of equity oriented mutual funds units are not taxable under India-UAE treaty

A resident of UAE earned STCG on sale of equity oriented mutual funds units in India. The taxpayer claimed exemption under Article 13(5) of the India-UAE DTAA.

AO denied claim by holding that underlying instrument of equity oriented MF is akin to a share, and STCG would be taxable in India as per article 13(4) of the DTAA. On appeal, CIT(A) deleted the addition. Aggrieved, Revenue filed appeal.

ITAT held that the term ‘share’ has not been defined in the DTAA. It referred to meaning provided under other allied Indian laws such as Companies Act, 2013, SEBI (Mutual Funds) Regulations, 1995 etc. and observed that “it is clear that ‘shares’ and ‘units of a mutual fund’ are two separate types of securities.” In view of the same, ITAT dismissed Revenue appeal.

Source: Dy. Commissioner of Income-tax (International Taxation), Kochi vs Sri K.E.Faizal Cochin ITAT ITA No. 423/Coch/2018 dated 8 July 2019

Tax payer treated as beneficial owner and eligible for India-Cyprus tax treaty benefits on interest income received

A Cyprus based company had earned interest income on Compulsorily Convertible Debentures (CCDs) from an Indian company and offered the income at beneficial rate of 10% under India-Cyprus DTAA. The Cyprus co. had received sum from its 100% holding company based in Mauritius, which held 99.5% in Indian co.

The AO denied treaty and taxed interest income at 40% by holding that Cyprus co. was not beneficial owner and that it was a back-to-back loan transaction.

Upon appeal, ITAT held that the mere fact that the CCDs were funded using monies received from its immediate shareholder does not make the arrangement a back-to-back transaction lacking economic substance. The tax payer had absolute control over the funds received and wholly assumed risk involved on CCDs.

Further, AO failed to prove that tax payer did not have exclusive possession and control over the interest income received; or it was required to seek approval from any entity to invest or it was not free to utilize the interest income received at its sole and absolute discretion, unconstrained by any contractual, legal, or economic arrangements with any other third party. The AO was directed to accept the return filed.

Source: M/s Golden Bella Holding Ltd v/s Deputy Commissioner of Income Tax (International Taxation), ITA No. 6958/Mum/2017 (Mumbai ITAT) dated 28 August 2019
High Court quashes order u/s 197 denying India-Mauritius tax treaty benefits

In the present case, capital gains had arisen to a Mauritius company, pursuant to sale of shares of an Indian company which was promoted by the assessee. The assessee filed an application for 'Nil' withholding tax certificate u/s 197 of the Act. AO rejected the application on ground that the transaction was not genuine and directed the payer to deduct tax.

HC noted the grandfathering clause under India-Mauritius DTAA and opined that prima facie assessee’s income arising out of sale of shares was not taxable in India. It acknowledged that, despite the existence of DTAA, availability of TRC and CBDT circular stating that TRC is valid as long as it is in operation for applying DTAA, there is no legal position laid down by SC that shuts out Revenue when it comes to fraudulent or fictitious transaction.

However, HC stated that the Revenue did not provide sufficient prima facie material to prove that the entire transaction was a sham and a colourable device. HC clarified that the mere fact that assessee has not transacted in any other business, could not produce TRC of the companies which hold shares in assessee, the extent of administrative expenditure and the employment structure by themselves may not be sufficient to demonstrate whether the transaction was a sham. HC held that these aspects can be examined at the time of assessment proceedings.

HC quashed AO's order denying 'Nil' withholding tax certificate and directed revenue to release the tax withheld subject to conditions.


Claim of loss and refund cannot be denied merely on grounds that the assessee had declared a positive income in the immediately preceding year.

For AY 2017-18, the assessee had claimed huge losses and refund thereon in the ITR filed. The AO withheld refund u/s 241A of the Act on the ground that in the immediately preceding AY, the assessee had declared positive income.

The HC held that merely because in immediately preceding AY assessee had declared a positive income as against substantial loss declared in relevant AY could not be a ground to doubt contents of return or claim of assessee with respect to loss suffered and withhold refund.

Further, the HC stated that an auto-generated communication containing note of withholding of the refund as per section 241A does not satisfy legal tests for withholding refund. HC directed the AO to release the refund with interest.

Source: Vodafone Idea Ltd vs DCIT [2019] 111 taxmann.com 451 (Bombay) dated 14 October 2019

Tax authorities cannot avoid processing of tax return u/s 143(1) of the Act and granting refund to taxpayer

The assessee filed income tax return for AY 2015-16. As per the Act, AO was required to process the return before 31 March 2018. On 27 March 2017, AO issued notice u/s 143(2) of the Act for initiating scrutiny assessment proceedings.

The assessee requested AO to process the return and issue refund, irrespective of scrutiny notice. The AO denied to issue the refund on the ground that refund could not be issued as notice u/s 143(2) was issued. The AO referred to draft assessment order, which, if finalised would give rise to a tax demand instead.

Aggrieved, the assessee filed a writ petition. HC held that none of the grounds are sufficient for income tax department to avoid processing of return and withhold the refund. HC directed the AO to process the return and release refund due, with interest.

Source: TATA communications Limited vs Deputy Commissioner of Income Tax Bombay HC Writ Petition No. 894 of 2019 dated 8 July 2019

Issuance of paper refunds and manual order upload functionality in Income Tax Business Application (ITBA) module

As per previous instructions issued by CBDT, refund arising out of manual orders which were uploaded in the ITBA were to be issued through the system. Manual cheques not to be issued by AO except in specific cases for which permission from Principal Director General of Income Tax (System) taken.

The process of seeking approval was taking substantial time at different stages of approvals and communication. In order to reduce time, permission would now be required from Chief Commissioner of Income Tax instead of Pr.DGIT(S) in case where there is no alternative except to issue paper refund.
Further, where refund could not be issued from system, including unavailability of functionality such as – refund to successor of business in the matter of amalgamation, refund to foreign national not having bank account in India etc. In such situations, request was received from AO for manual issuance of refund. The development of functionality is under consideration in such cases.

Due care and safeguard are required to be maintained to before issuing paper refund.

Source: CBDT Instruction F. No System/ITBA/Instruction/Assessment/177/16-17/ dated 18 June 2019

❖ TDS credit allowed in year where income is assessable and not year of TDS deposit

In respect of an invoice raised in March 2011, assessee claimed tax deducted at source (TDS) credit in FY 2010-11. However, it was appearing in Form 26AS in subsequent year as the deductor had deposited the TDS in April 2011. AO denied TDS credit to assessee.

ITAT held that TDS credit should be allowed in the year in which the corresponding income is assessable in hands of assessee and rejected Revenue’s stand that TDS credit can be given only in the year of deposit of TDS.


❖ Taxpayer allowed to file a revision petition against intimation in order to claim tax benefit which was not claimed in the return of income

A Spanish company had offered fee for technical services income earned in its return of income at the rate of 20% as per Article 13 of India-Spain DTAA, as against 25% under the Act. The return was accepted and processed u/s 143(1) of the Act.

As per protocol to the DTAA, further concessional rate of 10% was available. The assessee, subsequently filed revision petition u/s 264 to revise the intimation.

On filing writ petition, the HC stated that “Even though, this extra 10% paid by the Petitioner was of its own volition, it was indeed prejudicial to the Assessee/Petitioner.” It held that petition u/s 264 seeking revision of ‘intimation’ u/s 143(1) was maintainable and directed Revenue to permit assessee to revise its return and issue refund of the excess tax paid with interest.

Source: M/s Epcos Electronic Components S.A. v/s Union of India & Ors W.P. (C) 10417/2018 Delhi High Court dated 10 July 2019

❖ Paper return can be filed in case self-populated e-return restricts claim of loss set off

The prescribed self-populated ITR, to be filed electronically, did not permit assessee to raise a claim of set off of losses u/s 72 of the Act. There is no provision available with the assessee to filing a hard copy (paper copy) of ITR and AO cannot accept the ITR in paper form. Accordingly, if the assessee files the electronic ITR in the present available form, the assessee would be taxed on amounts which are not taxable and may face penal consequences or the return may be treated as defective. Therefore, the assessee approached the court to be permitted to file ROI in paper form.

The HC held that Rule 12 of Income-tax Rules, 1962 mandates electronic filing of ROI. However, the procedure of filing the ROI cannot bar an assessee from making a claim under the Act which he feels he is entitled to.

The HC directed assessee to file representation with CBDT before the return filing due-date and urged CBDT to expeditiously dispose the same and issue a clarification on this issue. The assessee was also directed to file return electronically as well as in paper form before the due-date and that AO to accept the paper return. Till CBDT takes a decision on the petitioner’s representation, the Revenue was directed not to act upon the electronically filed ROI so as to initiate any coercive recovery proceedings.

Source: Samir Narain Bhojwani v/s DCIT (Bombay HC) Writ Petition 2825 OF 2019 dated 22 October 2019

❖ SC quashes assessment carried without issuance of notice u/s 143(2)

The AO made additions during assessment to returned income. The assessee filed appeal challenging the ground of jurisdiction of AO regarding non-issuance of notice u/s 143(2).

ITAT held that issue of notice for completion of assessment was a statutory requirement and is not a curable defect u/s. 292BB of the Act. HC and SC confirmed order of ITAT and quashed assessment as no notice u/s. 143(2) was ever issued.

Source: CIT vs. Laxman Das Khandelwal (SC) Civil Appeal Nos. 6261-6262 of 2019 dated 13 August 2019

❖ Mere issuance of scrutiny notice is not a reason to withhold tax refund

The AO did not grant refund for AY 2017-18 on the ground that scrutiny assessment was initiated and in accordance with section 241A of the Act, the refund was withheld.
In response to writ petition filed, HC held that a notice issued u/s 143(2) of the Act is not a sufficient ground to withhold refund u/s 241A of the Act. In order to withhold refund, the AO is required to make an objective assessment of all the relevant circumstances that would fall within the realm of “adversely affecting the revenue” and obtain necessary approvals.

Source: Maple Logistics Private Limited & Anr. v. Pr. CCIT (Del HC) Writ Petition W.P.(C) 7063/2019 dated 14 October 2018

- **Intimation issued by CPC is appealable before CIT(A)**

Assessee was issued an intimation u/s 143(1) of the Act by CPC wherein certain disallowances were made. Against the intimation, assessee filed an appeal with CIT(A).

CIT(A) dismissed the appeal stating that no appeal lies against the intimation issued by CPC u/s 143(1) with a direction that assessee to file an online rectification application for necessary correction.

On appeal, ITAT remanded matter back to CIT(A) for fresh adjudication on merits stating that intimation is an appealable order and that there is no requirement in law to approach the CPC for rectification of the order, if the assessee is aggrieved by the order.

Source: Dixit Rice Mill v. DCIT ITA No. 373/Agra/2018 (Agra ITAT) dated 10 January 2020

- **CIT(A) cannot dismiss appeal against penalty on additions made in quantum proceedings**

CIT(A) had confirmed penalty levied by AO u/s 271(1)(c) of the Act merely on ground that the additions were confirmed in quantum proceedings.

On appeal, ITAT set aside penalty order and held that quantum proceedings and penalty proceedings are independent and distinct in nature. CIT(A) has to give reasons for its decisions while confirming or deleting the addition and directed the CIT(A) to re-decide the appeal.

Source: NIIT Ltd vs. DCIT (2019) 112 taxmann.com 66 (Delhi Trib) dated 1 November 2019

- **Bombay HC refuses entertaining assessee's challenge against reopening notice by Hyderabad based AO**

A UK company, having registered office in Mumbai was being assessed to tax regularly at Hyderabad, had PAN card at Hyderabad and never applied for transfer of PAN card.

The assessee filed a writ petition with Bombay HC challenging re-assessment notice issued by AO based in Hyderabad.

HC highlighted that the issue of the HC where the assessee was served with a notice getting a territorial jurisdiction to entertain a petition challenging such notice, is not free from doubt. It further stated that if assessee’s stand is accepted that since the re-assessment notice was served to it at Mumbai, a part of cause of action had arisen within the jurisdiction of Bombay HC, it would give rise to possibility of different legal principles being applied in case of the same assessee on the same issue and possibly in relation to the same AY.

HC stated that appeal against the original assessment would be governed by law laid down by Telangana HC and denied to entertain assessee’s writ. It directed assessee to move appropriate HC.

Source: HSBC Holdings PLC vs DCIT Writ Petition No. 3624 of 2018 (Bombay HC) dated 1 July 2019

- **To impose penalty for failure to disclose ‘interest on refunds, non-reflection of interest in Form 26AS is not relevant**

Taxpayer had not disclosed interest income received in the return of income filed. The assessee claimed that Form 26AS downloaded at the time of filing of return, did not disclose any interest on refunds.

ITAT observed that Form 26AS is a statement of tax deducted at source and the words NA reflected against ‘interest component of refunds’ in Form 26AS only meant information was ‘not available’, not Nil interest on refund. ITAT accepted Revenue’s reliance on refund advice reflecting interest income, which were served on assessee. ITAT confirmed penalty u/s 271(1)(c) towards non-disclosure of interest received on income-tax refunds.

Source: Neeraj Kumar vs ITO ITA 399/Ars/2017 (ITAT Amritsar) dated 23 May 2019

- **Mere non-disclosure of receipts doesn’t imply ‘income escapement’**

The company had filed a writ petition with HC against the issuance of re-assessment notice by AO.

In the present case, shares were sold for a consideration exceeding INR 300 crore. AO issued re-assessment notice holding that non-disclosure of sale consideration receipt by assessee in its return amounted to ‘escapement of income’.

Assessee contended that since LTCG was exempt no income chargeable to tax had escaped assessment.
HC allowed assessee petition and quashed re-assessment notice issued by AO holding that mere non-disclosure of receipt would not automatically imply escapement of income chargeable to tax.”

Source: The Swastic Safe Deposit and Investments Ltd. v. ACIT (Bom HC) Writ Petition No 1230 of 2019 dated 25 June 2019

❖ System lapse for refund irrelevant and computer system cannot override factual aspects

In the present case, the company withheld tax and erroneously showed the payment under old as well as new Tax Deduction and Collection Account Number (TAN) giving rise to TDS mismatch and demand which was to be corrected. Despite the officer agreeing that this is a system error and that the TDS demand of the company should be deleted from the system, it was observed that no steps were taken to delete the demand from the computer system.

In writ application filed, HC remarked that the computer system cannot override the factual aspects, i.e. “If the refund is payable, whether the computer systems accepts or not, is of no consequence.”

It held that the department cannot withhold the refund of assessee and directed Revenue to rectify the error of TDS mismatch in the computer system as expeditiously as possible and release of refund to assessee with statutory interest.


❖ Assessment can be reopened on basis of information obtained during course of earlier assessments

On the basis of information received during the course of assessment for AY 2015-16, AO issued notice u/s 148 for re-opening of assessment for AY 2017-18, the return of income for which had been processed by way of an intimation u/s 143(1) of the Act. Aggrieved, the assessee filed writ petition before HC challenging the notice.

HC dismissed the petition and held that notice was valid. HC stated that the reopening notice can be issued on the basis of information obtained during course of assessment for earlier AYs as the AO had no occasion to examine the claim of the assessee for AY 2017-18.

Source: Belazio Construction (P.) Ltd. vs. Income-tax Officer, Ward-12(1)(3) [2019] 111 taxmann.com 454 (Bombay HC) dated 23 August 2019

❖ Counsel’s outstation visit no ground to seek adjournment

In the present case, the learned counsel appeared on behalf of the counsel (out of station) for the appellants and submitted that the learned counsel for the appellants was not present in the Court as he was out of station. The court held that this was not a valid ground to seek adjournment and therefore rejected the request for adjournment.

Source: Ram Rimon Tripathi & Ors. Vs. State of U.P. & Ors – Civil Appeal No 9142-9144 of 2010 dated 7 February 2019

3. Miscellaneous Updates- other changes

❖ Toolkit for implementation of Beneficial Owner to tackle tax evasion released

The Secretariat of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) and Inter-American Development Bank released a toolkit for implementation of Beneficial Ownership to help tax administrations tackle tax evasion more effectively.

Member jurisdictions of the Global Forum can use it to implement legal and supervisory frameworks to identify and collect information on BO, which is now a requirement of the international standards. The aim of the toolkit is to foster understanding of BO contained in the international tax transparency standards. The Toolkit covers following key issues:

- Concepts and criteria to identify BO
- Technical aspects of BO requirements such as distinguishing between legal persons and legal arrangements, measures taken internationally to ensure availability of information on BO etc.
- Ways in which the principles on BO can play out in practice in Global Forum exchange of information on request peer reviews.
- Why BO information is a crucial component of the automatic exchange of information regimes being adopted by jurisdictions around the world.

Report dealing with profit attribution to Permanent Establishment

CBDT formed Committee to examine the existing scheme of profit attribution to PE under Article 7 of tax treaties and recommend changes in Rule 10 of the Income-tax Rules, 1962.

The Committee submitted its report and it was decided to seek stakeholder’s comments on the report. The report deals with issues relating to attribution of profits to a PE, the need to bring greater clarity and predictability in the applicable tax regime. Comments were to be provided within 30 days of the publication of report on Income Tax website.

Source: CBDT F. No.500/33/2017-FTD.I dated 18 April 2019

RBI released draft circular on liberalisation of hedging of foreign exchange risk

RBI revised the existing facilities for non-residents and residents to hedge their foreign exchange risk on account of transactions permitted.

The revised directions contain changes as follows:

- Definitions provided- anticipated exposure, contracted exposure, hedging and users
- General and specific directions provided for AD
- Directions for exchanges
- User Classification Framework provided. AD to classify users as either retail user or non-retail user.
- Eligible products:
  - **Retail user**: Forwards, purchase of call and put options (Only European options), purchase of call and put spreads, swaps.
  - **Non-retail users**: Any derivative contract, which the AD can price and value independently and is approved by the board of the AD, provided it is not a leveraged derivative.

All previous operational guidelines, terms and conditions to stand withdrawn.


The draft directions proposed to, inter alia, merge the facilities for residents and non-residents into a single unified facility for all users, allow users having valid underlying exposure to hedge flexibly using any instrument of their choice, introduce the ability to hedge anticipated exposure to foreign exchange risk. Necessary amendments to be notified.

Source: Draft Circular on Risk Management and Inter-bank Dealings: Hedging of foreign exchange risk by Residents and Non-Residents – Liberalisation on 15 February 2019

SEBI proposed framework for innovation sandbox and released framework for regulatory sandbox

SEBI proposed innovation sandbox in order to promote usage of FinTech which would impact development of securities market.

Under this, FinTech firms to have access to market related data, which is otherwise not readily available to them, to enable them to test their innovations before introduction in a live environment.

A steering committee to develop operating guidelines for the framework.

In this connection, SEBI has introduced a discussion paper on regulatory framework called ‘Regulatory Sandbox’. Under this, financial institutions regulated by SEBI are to be granted certain facilities and flexibilities to experiment with FinTech solutions in a live environment and on real customers.

The discussion paper aims to provide key principles and proposed approach for operationalizing the regulatory sandbox. Comments were to be provided latest by 18 June 2019.

4. Market Watch- select press articles

- **RBI expresses concerns over FPI-NRI route merger**
  
  RBI has expressed concerns over the market regulator’s proposal to merge investment route of NRIs with FPI route, said three people privy to the development. The central bank is against the plan in its current form because the regulations that govern both the modes of inflows are separate, and clubbing the two would cause a regulatory haze. RBI is concerned over what rules would apply to the non-market investments made by NRIs through the NRE route if they were merged with the foreign portfolio route.


- **Govt in talks with MSCI to ensure higher weightage**
  
  Top Indian officials are in talks with MSCI, a provider of globally tracked investment indices, to strengthen the country’s case for higher weightage on key gauges after suggested recasts to the matrix had threatened to lower the weighting instead of raising it in kilter with New Delhi’s economic profile.


- **4 years post safe harbour rules, eight FPIs to test waters in India**
  
  At least eight FPIs are looking to set up shops in India and manage global funds from the country, four years after the government introduced safe harbour rules. While the regulations still pose some tax related problems, these FPIs will station their fund manager in India to operate global funds.


- **FPIs shift to GIFT City, boost market moves**

  Many FPIs are shutting operations in tax havens like Mauritius, Singapore and Dubai to set up shop in Gujarat’s GIFT City.


- **IT dept to issue only e-refunds from Mar 1, 2019; bank account-PAN linking must**

  The income tax refunds will be credited only to bank accounts (savings/current/cash/OD) which are linked to PAN, w.e.f. March 1, 2019. Income tax department will issue only e-refunds and that too these will be credited only to bank accounts linked with PAN.


- **RBI eases norms for FPI special window**

  India’s central bank on Friday eased norms for FPI buying debt assets under a special window amid expectations that overseas funds would increase allocations to Mumbai after the ruling combine’s return to power with a bigger majority. RBI removed a mandatory investment cap, exempting investors from bringing in at least a fourth of the limits purchased through the VRR within one month.


- **India will decide on sharing daily US dollar-Rupee rate with overseas exchanges**

  India will soon have to take a call on whether to officially share the US dollar-rupee reference rate with overseas exchanges, fund houses, corporates and banks. The benchmark rate is used to settle millions of trades and currency derivative contracts in India and abroad.


- **Sebi hit the brakes on ‘free of cost’ transfers for FPIs in past year**

  An FPI could earlier transfer assets between its arms, in the wake of a merger of schemes or similar reorganisation, through an application to the markets regulator. SEBI has not been giving permission to FPIs to transfer assets through a provision which was previously in common use.


- **Direct Tax Code: All you need to know about govt panel’s recommendations**

  While not many details about the report have emerged, the committee has highlighted the need to review existing tax brackets, surcharges and implementation of special guidelines for startups. The committee’s suggestions could make the existing Income Tax Act friendlier and even reduce the burden for middle-income group taxpayers.

  [Source](https://www.indiatoday.in/business/story/direct-tax-code-all-you-need-to-know-about-govt-panel-s-recommendations-1582646-2019-08-20) - 20 August 2019
Proposed NSE IFSC-SGX Connect gets regulatory nod

The proposed NSE International Financial Service Centre (IFSC)-SGX Connect aims to bring together the trading of Nifty products to Gujarat International Finance Tech-City (GIFT) and create a larger pool of liquidity, comprising international and home market participants, NSE said in a release.

Sebi plans rules for advisers, PMS to operate in GIFT City

The market regulator plans to come out with guidelines for investment advisers and portfolio management services (PMS) to enable them to provide services at the IFSC in Gandhinagar. It is also considering allowing trading of new products like dollar-rupee derivatives in India’s first IFSC.

RBI panel: Allow FPIs to buy bad loans directly

In order to address the issue of possible volatility that may emerge by allowing foreign players, a scheme similar to that of the Voluntary Retention Route for FPI investments in debt markets may be envisaged, the task force suggested.

High-level panel to study merger of NRI & FPI routes

The government plans to appoint a high-level committee to look into merging the NRI and FPI routes. Finance minister Nirmala Sitharaman had announced in the July budget that the investment avenues would be merged to give NRIs seamless access to Indian equities.

Fresh bonanza for stock markets? Dividend distribution tax may be scrapped

A bonanza is in the offing for stock markets as the Prime Minister’s Office and the Finance Ministry are working on measures which may include dividend distribution tax to be scrapped and review of existing slabs and holding period of long-term capital gains, short term capital gains and STT.

Tax officials express concerns over efficacy of faceless Income Tax assessment

Tax officers have expressed concerns over the faceless income tax assessment system initiated by the CBDT, saying it will create procedural difficulties and may hit revenue collections. The assessing officers will face difficulties and will not be able to make proper assessment without looking into books of accounts of taxpayers.

Indian companies can now use the international stock exchanges operating out of GIFT City in Gujarat to list their depository receipts

This in a way is expected to enable the Indian companies increase access to foreign funds through the listing of global/American depository receipts in a market closer home, say capital market observers.

Foreign investors keen on REITs, InvITs: Sebi

Sebi Chairman Ajay Tyagi and other officials met scores of foreign investors in the US and saw keen interest from them in emerging areas such as REITs and InvITs, which have a total asset size of more than USD 10 billion.

Sebi tightens rules on P-notes, to need separate registrations

Sebi said late Tuesday that FPI would have to make separate registrations for issuing p-notes for underlying derivatives. However, this requirement is waived for p-notes against underlying cash equities.
Many investors make Singapore their base now

VCC is a new legal entity form or structure for all types of investment funds in Singapore. It can be formed as a single standalone fund, or as an umbrella fund with two or more subfunds, each holding different assets.


Income Tax task force report suggests complete rejig of tax slabs, saving govt Rs 55,000 crore

The government could boost its revenues by more than Rs 55,000 crore if it implements a task force report that calls for a complete rejig of income tax slabs and capital gains tax regime, two persons familiar with the content of the report said.


Budget 2020: FinMin seeks industry inputs on direct, indirect tax changes

The finance ministry for the first time has sought suggestions on changes in direct and indirect tax rates from the industry. This comes at a time when a revenue shortfall and consumption slowdown are threatening to upset the government’s finances.


Market players want FM Sitharaman to rationalise taxes on equity

In the three-hour-long pre-Budget meeting with Finance Minister, various stakeholders and regulators discussed key proposals including rationalisation in the tax rates on the equity markets, boosting the growth of certain categories of AIFs and alleviating the stress in the mutual funds industry.


Budget 2020: Centre may announce increase in FPIs’ debt limit to 10%

The Centre is considering increasing the government bond investment limit of FPIs to at least 10 per cent of the outstanding, from 6 per cent now, with an aim to incorporate local bonds into the global indices, according to sources close to the matter. The decision may be announced in the upcoming Budget.


Pension, sovereign funds bring in more ‘sticky’ money

The share of long-term ‘sticky’ foreign funds including global pension funds, sovereign wealth funds, central banks and government agencies in Indian equities has been on the rise despite wobbly economic parameters in 2019.


NRIs may soon get to invest as FPIs

Non-resident Indians (NRIs) will soon be able to invest in Indian markets as foreign portfolio investors (FPIs). Sebi is planning to create a third category of investors under the current FPI regime for NRIs to invest in the local markets, said two people aware of the development.


New Singapore treaty harsher than GAAR, may impact FPI flows into India

Singapore might lose some of its allure for various foreign portfolio investors as a preferred destination to route their investments into India. With the Multi-Lateral Agreement (MLI) between the two countries set to come into force from April 1, fund managers in Singapore, who invest in India, could face a stiffer task of convincing local tax authorities that they have not set up shop in the island nation to avail the tax benefits.


Govt Mulls no Tax on LTCG with 2-year Holding Period

The government has approached tax advisers and experts on the possible implications of removing tax on long term capital gains (LTCG) introduced amid much criticism in the FY19 budget. Government officials, tax advisers say, are considering options to attract more foreign long-term investment and one proposal is to do away with LTCG tax on listed equities.

The government may also tweak the definition of ‘long term’ from a year to two years, people with knowledge of the discussions said. Currently, 10% tax is levied on LTCG.

5. Market Trends - relevant to FPIs

- **Country wise AUC of FPI (in USD billion) in India as on 31 Dec 2019**

<table>
<thead>
<tr>
<th>Country</th>
<th>AUC (USD billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>NETHERLANDS</td>
<td>12</td>
</tr>
<tr>
<td>NORWAY</td>
<td>12</td>
</tr>
<tr>
<td>JAPAN</td>
<td>17</td>
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<td>CANADA</td>
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<tr>
<td>IRELAND</td>
<td>18</td>
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<td>UNITED KINGDOM</td>
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<td>SINGAPORE</td>
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<td>LUXEMBOURG</td>
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<tr>
<td>MAURITIUS</td>
<td>62</td>
</tr>
<tr>
<td>Other</td>
<td>80</td>
</tr>
<tr>
<td>UNITED STATES OF AMERICA</td>
<td>167</td>
</tr>
</tbody>
</table>

Source: NSDL website
AUC comprises of Equity, Debt and Hybrid investments

- **Trends in FPIs monthly inflows/ outflows Investment (in INR crores) – Dec 18 – Nov 19**

Source: SEBI Bulletin – Dec 2019

- **Trends in Number of FPI registrations – Jan 19 – Dec 19**

Source: NSDL website
FPI Debt Utilisation Limit as on 27 Jan 2020

Limit in Corporate Bonds in USD Billion
- Limit Available, 18.95
- Limit Utilised, 26.33

Limit in Government Securities in USD Billion
- G-Sec - General: Limit Utilised 25.07, Limit Available 10.08
- G-Sec - Long Term FPIs: Limit Utilised 12.13, Limit Available 4.31
- SDLs - General: Limit Utilised 8.59, Limit Available 0.16
- SDLs - Long Term FPIs: Limit Utilised 1.01

Source: NSDL website
Source: CCIL website

Bloomberg’s survey on easier market access of India

Investors’ call
Ease of access to India’s financial markets vs other markets
- Much easier: 2%
- Somewhat easier: 4%
- The same: 18%
- More difficult: 18%
- Much more difficult: 58%

Capital controls are the greatest barrier
- Capital controls: 37%
- Market liquidity: 22%
- Price discovery: 10%
- Lack of electronic access: 14%
- Others: 17%

Main challenges in accessing India’s financial markets

The path to greater participation
- Clearer regulatory guides: 43%
- New account processes: 20%
- Internationalization of bond market: 17%
- Ease of FX compatibility: 11%
- Electronic trading access: 4%
- Better research: 2.5%
- Better corporate governance: 2.5%

Ease of access key to boosting participation
- 92% said they would increase participation in India if access was easier

Source: Bloomberg Whitepaper