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kcm Insight

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Dear Reader,

We are happy to present kcmInsight, comprising of important updates in the legislative changes in direct tax law, corporate & other regulatory laws, as well as recent important decisions on direct taxes and transfer pricing matters.

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

Coverage

Detailed Analysis

Abbreviations

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

Coverage | Detailed Analysis

Corporate Tax

Important Rulings

- Bombay HC quashes reassessment proceedings, interprets first proviso to section 149, validity of issuance of notice by JAO
- Premium on redemption of unlisted NCD's taxable as interest income and not Capital Gains
- Additions made solely by relying only on CBIC information without any independent inquiry is unsustainable.
- Assessing Officer is bound to consider the reply filed by the Assessee before passing the assessment order
- Levy of penalty u/s. 270A of the ITA without mentioning the specific limb under which it is levied – Order liable to be quashed.

International Tax

Important Rulings

Indian Rulings

- Guarantee charges not derived from a debt or claim does not qualify as 'interest' under Article 12 of India-UK DTAA
- ITAT denies MFN benefits, classifies management fees and social security reimbursements as FTS
- Revenue from Software License and AMC Charges linked to the license not taxable as FTS / FIS
- UK LLP, a fiscally transparent entity, entitled to treaty benefits for pre-protocol amendment years
- Legal & Professional Services for product registration not taxable as no technology made available
- ITAT confirms India-Cyprus DTAA benefits, recognizes Taxpayer as "Beneficial Owner"

International Tax

Important Rulings

Foreign Rulings

- ORAs treated as Equity; Issuance Costs non-deductible against PE Profits under Netherlands-France DTAA

Important Updates

Foreign Updates

- UAE FTA issues Corporate Tax Guide on Business Restructuring Relief
- IRBM publishes Revised Tax Guidelines on Gains from Disposal of Foreign Capital Assets
- Administrative Measures for management of Beneficial Owner Information
- ATO issues Taxpayer Obligations for Withholding Tax on Payments to Non-Residents
- Streamlining Transfer Pricing: Malaysia's Updated APA Application Process

Transfer Pricing

Important Rulings

- Assessing Officer is obliged to pass draft assessment order under section 144C(1) even in partial remand proceedings
- Segregation of the milk from the water is necessary for ALP determination / Actual length of the controlled connection to be considered for the determination of ALP
- Netting off of outstanding balances prohibited on an entity level basis / Netting off of outstanding balances shall be carried out qua AE

Corporate Laws

RBI Notifications

- Fair Practices Code for Lenders – Charging of Interest
- Risk Management and Inter-Bank Dealings: Amendments
- Margin for Derivative Contracts
- Master Direction – Reserve Bank of India (Margining for Non-Centrally Cleared OTC Derivatives) Directions, 2024
- Issuance of partly paid units to persons resident outside India by investment vehicles under Foreign Exchange Management (Non-debt Instruments) Rules, 2019
- Launch of PRAVAAH, RBI Retail Direct Mobile Application and FinTech Repository

SEBI Notifications

- Flexibility to Alternative Investment Funds (AIFs) and their investors to deal with unliquidated investments of their schemes
- Nomination for Mutual Fund Unit Holders – exemption for jointly held folios

Corporate Laws

SEBI Notifications

- Facilitating collective oversight of distributors for Portfolio Management Services (PMS) through APMI
- Portfolio Managers - Facilitating ease in digital on-boarding process for clients and enhancing transparency through disclosures
- Periodic reporting format for Investment Advisers
- Certification requirement for key investment team of manager of AIF
- Framework for considering unaffected price for transactions upon confirmation of market rumour
- Audiovisual (AV) presentation of disclosures made in Public Issue Offer Documents
- Modification in Staggered Delivery Period in Commodity Futures Contracts

MCA Notification

- Relaxation of additional fees and extension of last date of filing of Form LLP BEN-2 and LLP Form No. 4D under the Limited Liability Partnership Act, 2008

Important Rulings

Bombay HC quashes reassessment proceedings, interprets first proviso to section 149, validity of issuance of notice by JAO

Hexaware Technologies Limited Vs. ACIT Mumbai, PCIT Mumbai, PCCIT Mumbai, CBDT New Delhi, Union of India, WP No. 1778 of 2023, Bombay HC

The Taxpayer is engaged in information technology consulting and software development and business process services, and it had filed return of income claiming deduction u/s 80JJAA and u/s 10AA of ITA. The said return was selected for scrutiny assessment. Subsequently the jurisdictional AO (JAO), passed the assessment order accepting the returned income.

After 3.5 years, the JAO issued notice under the erst while section 148 of the ITA (before its amendment vide the F.A 2021) on April 8, 2021. Aggrieved, the Taxpayer filed writ petition challenging the validity of notice on the ground that it was issued under old 148 provisions applicable up to March 31, 2021. The Bombay HC allowed the petition and termed the notice as invalid. However, the matter reached the SC and the Apex court in case of Union of India vs. Ashish Agrawal treated the issuance of notice as valid and such notice was deemed to be issued as notice issued u/s 148A(b) of the amended 148 provisions.

In view of the SC's aforesaid ruling the reassessment proceedings took place and the JAO passed order u/s. 148A(d) and issued notice u/s. 148 of the ITA on August 27, 2022. Aggrieved, the Taxpayer preferred a writ petition before the Bombay HC challenging the validity of the notice issued u/s 148 of ITA for AY 2015-16. The writ was filed on multiple legal grounds as well as on merits of the case. The contentions of the Taxpayer were:

i. Notice issued u/s 148 of the ITA was time barred in view of 1st proviso to section 149 of the ITA and

ii. Notice issued u/s 148 by the JAO is invalid since he had no jurisdiction to issue such notice after the Faceless Assessment scheme was notified

iii. Principle of change of opinion barring re-assessment still applies under amended provisions of section 148

iv. Deduction consistently allowed in past years cannot be subject matter of re-assessment and

v. Notice issued without DIN is considered as illegal and invalid.

With respect to the 1st contention, the Taxpayer contended that as per grandfathering provisions contained in first proviso to section 149, time limit for issuance of notice u/s 148 for the AY 2015-16 expired on March 31, 2022 (6 years from the end of assessment years as per old provision of section 148) and therefore the present notice issued by the JAO is time barred and hence bad in law. However, the revenue contended that the phrase "at that time" for issuance of notice used in first proviso to section 149 refers to April 01, 2021. Since for AY 2015-16, such time limit of six years is not expired on April 1, 2021, notice for such assessment is valid.

The Bombay HC held that the expression "at that time" used in first proviso to section 149 of the ITA refers to the date on which the notice was issued. Thus, on the date of issue of notice u/s 148, if a notice u/s 148 could not have been issued in view of limitation given in erstwhile section 149(1)(b) of ITA, for AY 21-22 or earlier, notice cannot be issued under the new 148 provisions as well. It was held that the revenue's

Important Rulings

contention that grandfathering provisions in section 149 will apply only to AY 13-14 & AY 14-15 is misplaced and not valid. Therefore, the HC held that the notice issued by the JAO for the AY 2015-16 was time barred.

Now with regard to the Taxpayer's second contention, the revenue argued that as per the CBDT guidelines dated August 1, 2022, the JAO was required to issue the notice and not the Faceless Assessing Officer (FAO) as the format required designation and physical signing of the AO. Subsequent to issue of such notice by JAO, FAO will carry out proceedings in faceless manner. The revenue also contended that the JAO and the FAO assumed concurrent jurisdictions and thereby the notice u/s 148 was valid.

The court held that the guidelines relied on by the revenue are for internal purposes of the department and are not issued u/s 119 of the Act and thereby such internal guidelines are not binding on the Taxpayer. Further, as per the faceless scheme framed by CBDT u/s. 151A of the ITA, it was the FAO who was required to issue the notice u/s 148 of the Act. Ruling in favor of the Taxpayer, the court held that the internal guidelines of the CBDT cannot override the scheme and hence reassessment proceedings were bad in law and were invalid.

The High Court further held that disallowance u/s 80JJAA cannot be regarded as 'asset' or 'expenditure in respect of transaction or in relation to event or occasion' or 'entry in the books' and therefore in view of section 149(1)(b), since AY 2015-16 falls beyond period of 3 years, no notice u/s 148 can be issued. The High Court further reiterated principle that the re-assessment initiated for in respect of the issue which has already been dealt by AO during original assessment proceedings amounts to change of opinion and thus makes proceedings invalid. The Court upheld the mandatory test of 'change of opinion' even under new provisions of section 148 of the Act.

With regard to issue of validity of notice issued without mentioning DIN, the High Court held that notice cannot be considered as valid in absence of valid DIN mentioned in notice and separate letter / intimation mentioning DIN cannot validate such notice since same is not in accordance with CBDT Circular No 19 of 2019 mandating mentioning of DIN in every notice issued by department.

The judgement brings a huge sigh of relief for Taxpayers with regard to the interpretation of the phrase "at that time" used in first proviso to section 149 of the ITA which was under dispute with the Income-tax authorities since the introduction of the new 148 provisions. The decision is also helpful to challenge the invocation of section 148 to disallow the claim of deduction/exemption if three years period has expired from the end of assessment year. With regard to issuance of notice u/s 148 by JAO, it shall likely to have impact on validity of all existing proceedings u/s 148 since in major cases notices u/s 148 have been issued by JAO and not in faceless manner. Considering large impact of above interpretations by Bombay HC in many on-going proceedings, the matter is likely to reach before Apex Court to decide validity of such principles held by HC.

Premium on redemption of unlisted NCD's taxable as interest income and not Capital Gains

Khushaal C. Thackeresy v. ACIT ITA No. 3679/Mum/2015 (AY 2010-11)

Important Rulings

The Taxpayer is an individual and was engaged in the business of trading in shares & securities along with being a director in a certain entity. During the AY 2010-11, he had declared long term capital gains on redemption of Non-Convertible Debenture (NCDs) and claimed exemption u/s 54F and 54EC of the ITA while filing his return of Income. The matter came under scrutiny assessment and the AO denied the benefit of deduction u/s 54F of the Act on the pretext that the Taxpayer has not got possession of the flat within the prescribed period of 3 years.

Aggrieved, the Taxpayer filed an appeal before the CIT(A) who saw the case from a different dimension and took a view that the income earned on redemption of NCDs would be taxable in the hands of Taxpayer as "interest income" and not under the head "Capital Gains. Further since such income was to be treated as interest income, there is no question of granting deduction u/s 54F / 54EC of the Act.

Aggrieved, by the said decision, the Taxpayer filed an appeal before the ITAT and contended that premium received on redemption of NCDs shall be taxable under the head of Capital gain considering that Debentures are a capital asset and its redemption results in extinguishment of rights. Further, the gain arising on transfer of Market Linked Debenture (MLD) is specifically taxable under the head capital gain as per Section 50AA and thereby redemption of debentures shall also be covered under the head "Capital Gains". Moreover, the Taxpayer drew a reference to various judgements wherein it was held that redemption proceeds of preference shares is subject to tax under the head of capital gains and thereby redemption premium of NCDs shall also be taxable under the head of Capital gain.

On the other hand, the Revenue contended that NCDs are debt instruments and are a way of borrowing money, thereby when such NCDs are redeemed at a premium, the said premium amount is essentially interest which shall be taxable as "interest income" and not "capital gains". Further, reference was made to circular No. 2 of 2002 wherein it was stipulated that in case of Deep Discount Bond, difference between the redemption price and the cost of purchase of bond shall be taxable as interest income or business income.

The ITAT upholding the order of the CIT(A) held that unlike preference shares, debentures are essentially debt securities, and its redemption is a repayment of debt and not extinguishment of rights. Further, section 50AA is applicable to only MLD's since the interest payable on them is not determined at the time of issuing the NCDs and their return is based on performance of underlying market index, thereby the tax treatment specified for MLD cannot be considered for debentures redeemed at a premium. Thereby the premium received on redemption of NCDs is to be taxed as "interest income". The Court has further observed that capital gains can arise in case of NCDs if they are sold in open market viz. gain arising from sale of listed NCDs. However, in present case, NCDs are private placed and not listed on any recognized stock exchanges and thus, income would taxable as 'Interest Income' and not 'capital gains'.

The above judgement in the context of unlisted NCDs provides a fundamental understanding regarding the nature of income earned when NCDs are redeemed at a premium. The tax treatment on redemption on debentures shall be essential to Taxpayers who consider to make

Important Rulings

investment in NCDs specially when the ITAT has held that premium on redemption would be taxed as "interest income" and not under the head "Capital gains".

Additions made solely by relying only on CBIC information without any independent inquiry is unsustainable.

Bausch and Lomb India Private Limited Vs. Assessment Unit, NFAC, Delhi, WP. (C) 5768/2024 CM APPL. 23894/2024, Delhi HC

The Taxpayer is a well-known brand in the eye care segment with all its purchases being imported. The case of the Taxpayer was selected for scrutiny assessment for AY 2022-23 wherein the AO observed that the total amount of purchases as reported by the Taxpayer were less vis-à-vis the amount of purchase as per the import information received from Central Board of Indirect Taxes and Customs (CBIC).

During the course of the Assessment proceedings the Taxpayer had asked the AO to provide it with the date wise bill of entry import information available with the AO, basis which the Taxpayer would be able submit its response. However, the AO rejected the Taxpayer's argument by stating that CBIC was the Apex body which deals with imports and its authenticity is unquestionable. The AO proceeded with an addition of such excess amount of purchase u/s. 69C of the Act as unexplained expenditure.

Aggrieved with the same, the Taxpayer preferred a writ petition before the Delhi HC on the ground that proper opportunity was not granted to it to contest the addition. The HC observed that the AO had simply relied on the information of CBIC by only providing the Taxpayer with cumulative import values without making any reference to bill of entry or its date. Thereby even the AO had no knowledge as to which imports were not disclosed by the Taxpayer and in absence of such identification the AO could not make an addition of unexplained expenditure u/s 69C of the ITA.

It further opined that the Taxpayer could not be faulted for not reconciling the data as information available with the AO is insufficient for carrying out any reconciliation exercise and if the AO wanted to make an addition on account of unexplained expenditure, he has to apprise himself as to details of such expenditure. Thereby the writ was allowed and the matter was remanded back to the AO.

The aforesaid judgement makes it clear that that the revenue authorities are required to independently evaluate and assess the information received from the external sources before taking any action against the Taxpayers. For making an addition on account of unexplained expenditure u/s 69C of the Act, the revenue authorities need to identify and satisfy themselves about the expenditure made by the Taxpayer. In absence of such identification and quantification, the addition is not sustainable.

Assessing Officer is bound to consider the reply filed by the Assessee before passing the assessment order

Chatursinh Javanji Chavda vs. Assistant Commissioner of Income Tax, 162 taxmann.com 466, Gujarat HC

The Taxpayer is an individual and had filed his return of income for the AY 2018-19. Subsequently, on account of search proceedings carried out in the premises of a third party, certain material was found against the Taxpayer.

Important Rulings

In view of the same, the AO reopened the case by issuing a notice u/s. 148 of the ITA.

Thereafter the AO issued notice u/s. 143(2) and 142(1) of the ITA calling for certain information which were furnished by the Taxpayer. Subsequently, the AO on February 13, 2024, issued show cause notice ("SCN") proposing addition to the total income of the Taxpayer. In accordance with the notice, the Taxpayer was required to submit his reply till by February 16, 2024

Since the Taxpayer was in the course of gathering the relevant materials and information, he filed an adjournment letter requesting the matter to be adjourned till February 23, 2024. Thereafter, the Taxpayer filed his detailed reply in response to the show cause notice on February 23, 2024. However, the AO without considering the reply to the SCN, passed the reassessment order on February 28, 2024, by merely stating that no reply / adjournment request was received from the Taxpayer in response to the SCN, thereby the assessment was finalised based om the material available on record.

Aggrieved by the reassessment order, the Taxpayer filed a writ petition before Hon'ble Gujarat HC. The court looking to the facts of the case held that since the Taxpayer had filed an adjournment and subsequently tendered its reply to the SCN, it was incumbent upon the AO to consider such reply and thereafter to pass the Assessment order by dealing with the objections raised by the Taxpayer. The court quashed and set aside the reassessment order passed by the AO and remanded the matter back to the him with a direction to consider the reply filed by the Taxpayer and provide him an opportunity of hearing.

The above judgement emphasises the intention of the National Faceless Assessment Scheme which is to provide an equal footing to the Taxpayer and the revenue in the litigation proceedings. The court has reiterated the cardinal principal that the "opportunity" provided to that Taxpayer should not be a mere "paper opportunity" and the responses of the Taxpayer ought to be considered by the revenue before "finalising" the Assessment orders.

Levy of penalty u/s. 270A of the ITA without mentioning the specific limb under which it is levied – Order liable to be quashed.

M/s. Enrica Enterprises Pvt. Ltd Vs. The DCIT, Central Circle 3(4), Chennai, ITA No. 1166&1167/Chny/2023, Chennai ITAT

The Taxpayer is engaged in business of manufacturing and sale of Indian Made Foreign Liquor. The income-tax authorities conducted search and seizure operations at the premise of Taxpayer and recovered large sums of cash. The director of the Taxpayer in his sworn statement u/s. 132(4) of the ITA explained the modus operandi of generation of unaccounted cash by inflating expenditure in the books of the Taxpayer. He also provided the year wise detail of unaccounted cash generated and the Taxpayer offered the same to tax while filing its return of income u/s 153A of the Act. The AO basis the Taxpayers admission passed the Assessment order accepting the Taxpayer's claim of additional income. In the said order, the AO also initiated the penalty proceedings u/s. 270A of the ITA.

In view of the same, a show cause notice was issued to the Taxpayer u/s. 274 r.w.s 270A of the

Important Rulings

ITA wherein the Taxpayer was asked as to why penalty should not be levied for "under reporting of income and under reporting as a consequence of misreporting of income". The Taxpayer had furnished its reply stating that show cause notice was invalid since the AO had not specified any charge for which penalty shall be levied i.e. whether penalty was for under reporting of income or for misreporting of income. However, the AO passed the penalty order by imposing penalty on the Taxpayer.

Aggrieved with the same, the Taxpayer preferred an appeal before the CIT(A) which upheld the order of the AO. The Assessee challenged such order before the Chennai ITAT.

The ITAT observed that provisions of section 270A of the ITA has two limbs or two charges for which penalty can be levied i.e. under reporting of income or for misreporting of income. Before initiating penalty proceedings, the AO is required to arrive at satisfaction that for which charge he wants to initiate the proceedings. The AO had failed to issue a proper notice specifying such charge and therefore it vitiated the entire proceedings since the Taxpayer was not given proper opportunity to explain its case on a specific charge.

Further on merits of the case, the ITAT held that assessment proceedings and penalty proceedings are two separate proceedings. The finding in assessment proceedings cannot be considered as conclusive for the purpose of levying a penalty and the AO must conduct independent findings to arrive at a satisfaction as to is this a case of underreporting or income or misreporting of income. In the present case the AO had confirmed the penalty addition purely on the basis of sworn statement of the Taxpayers directors with no independent findings. Therefore, the ITAT held that penalty levied by the AO is unsustainable in law.

The above judgement emphasizes on the fact that it is the responsibility of the AO to arrive at satisfaction under which limb of section 270A is the penalty leviable in the case of the Taxpayer. Further the finding from the assessment proceedings can be the base but cannot be the sole ground for initiating the penalty proceedings. The AO is bound to carry an independent inquiry and it does not follow that penalty is mandatory whenever addition or disallowance is made in assessment proceedings.

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

Indian Rulings

Guarantee charges not derived from a debt or claim does not qualify as 'interest' under Article 12 of India-UK DTAA

Johnson Matthey Public Limited Company [ITA Nos. 727/2018 – Order dated 28 May 2024 (Delhi HC)]

Taxpayer, a tax resident of UK, engaged in the manufacture of specialty chemicals, extended guarantees to various overseas branches of foreign banks on a global basis in relation to credit facilities extended by those financial institutions to its Indian subsidiaries pursuant to Intra Group Parental Guarantee and Indemnity Services Agreement and received guarantee charges in lieu of the same. The taxpayer offered the guarantee charges as 'interest income' taxable under Article 12 of India-UK DTAA. The AO and DRP rejected the taxpayer's contention and held the income from guarantee charges to be taxable as 'Other Income' as per Article 23 of India-UK DTAA.

The key issue before the Delhi High Court was whether the guarantee charges constituted 'interest' income under the Act and Article 12 of the DTAA, and whether this income accrued or arose in India.

The Delhi High Court concluded that the guarantee charges did not qualify as 'interest' income and accrued in India for the following reasons:

- Payment or re-payment pursuant to any loan to be qualified as "interest" had to be within the context of loan and should relate to the parties to the privity of contract. The taxpayer was not a party to the loan transactions, and the contract of guarantee was separate from the loan contract.
- The guarantee charges were not for any debt owed to the taxpayer by its Indian subsidiaries. They were compensation for the service of providing a guarantee to overseas financiers, ensuring credit facilities to the Indian subsidiaries.
- As per the Act, interest pertains to amounts payable in respect of monies borrowed or debts incurred. The debt in question was not owed to the taxpayer by the Indian subsidiaries. The income was for potential liability that could possibly befall the taxpayer if its Indian subsidiaries defaulted.
- The obligation to pay the guarantee charges was incurred in India, was in respect of services utilized in India and was agreed to arise with regularity as per the stipulations forming part of the Intra Group Agreement. Therefore, the income accrued in India. The argument that the risk was ultimately borne by the taxpayer outside India where its overseas assets might be impacted if the guarantee were to be enforced was held to be irrelevant for determining where the income arose or accrued.

The HC in this case has disagreed with the view taken by Hon'ble Mumbai ITAT in the case of Capgemini SA v. ADIT [IT Appeal No. 7198 (Mum.) of 2012, dated 28-3-2016] where evaluating similar facts, the Mumbai Tribunal held that guarantee charges for guarantee given by non-resident outside India did not accrue in India and hence not taxable under 'Other Income' Article of DTAA. The said view was followed by Chennai Tribunal in the case of Daechang Seat Co. Ltd. [2023] 152 taxmann.com 163 (Chennai - Trib.)]. With the Delhi HC taking a different view it would be interesting to note the stand taken by judiciary in different states upon this issue.

Important Rulings

ITAT denies MFN benefits, classifies management fees and social security reimbursements as FTS

JCDECAUX S.A. [ITA No. 2473/Del/2022 – Order dated 3 May 2024 (Delhi ITAT)]

Taxpayer (tax resident of France) received consideration from JCD Advertising India Private Limited ('JCD India') towards A) provision of management services B) provision of corporate guarantee to foreign banks for borrowings by JCD India and C) reimbursement of social security contribution in France. AO treated the aforesaid receipts as taxable under the Act as well as DTAA and denied the benefit of MFN clause contained in India-France DTAA whereas the taxpayer treated the receipts on account of management services as not taxable in India by invoking the restricted definition of FTS as contained in India-UK DTAA and contended that the said services did not make available technical knowledge, experience, skill, know-how etc. nor any technology had been made available to JCD India.

In Appeal, Hon'ble ITAT denied the benefits of MFN clause relying upon the decision of Supreme Court in case of Nestle SA (Civil Appeal Nos. 1420 to 1432/2023) wherein Hon'ble Court held that a notification u/s 90(1) is necessary requirement and a mandatory condition for invoking the MFN clause. Similarly, the ITAT upheld the addition of reimbursement of expenses relating to social security contribution as FTS by relying upon Delhi HC judgment in the case of Centrica India, wherein it was held that the term 'reimbursement' could not be determinative of the nature of the payment and even the fact that no mark-up was charged by the overseas entity over and above the costs of the seconded employees could not negate the nature of the transaction. Delhi ITAT in another recent judgement in the case of *Advics Co., Ltd. [ITA No. 1053/Del/2022]* had ruled in favor of the taxpayer where part salary was disbursed in the home country of expats and reimbursed by Indian entity. Readers may refer to KCM Insights for the month of April wherein the said judgement has been summarized.

The Supreme Court in its decision in case of Nestle (supra) laid down that issuing a notification by Indian Government is a mandatory precondition for implementation of the MFN clause in the Tax Treaties. In the context of India-France DTAA, the language of the protocol in Treaty itself states that it forms an integral part of the treaty and provides for automatic application of MFN clause without requirement of any further negotiation / notification / agreement. Accordingly, by virtue of the specific language of the protocol which forms an integral part of the treaty, ideally India does not have a choice to issue selective notification to restrict / limit the benefit as agreed in the treaty. Nevertheless, review petition has been filed by petitioners in case of Nestle SA and same is pending before Supreme Court for disposal.

Revenue from Software License and AMC Charges linked to the license not taxable as FTS / FIS

Openwave Mobility, Inc. [ITA No. 1644/Del/2022 – Order dated 1 May 2024 (Delhi ITAT)]

Taxpayer, a US tax resident, entered into Software License Agreement with Reliance Jio Infocomm Ltd (RJIL) for transmission control protocol and video optimization solution in India. It also entered into a Service Level

Important Rulings

Agreement by way of an Annexure to the Software License Agreement for providing annual maintenance and support services pursuant to which the assessee received software licensing income and Annual Maintenance Contract (AMC) service income. The AO classified the receipts as taxable as FTS.

The Dispute Resolution Panel (DRP) determined that the software license fees were business income, not royalty, and thus not taxable in India without a PE relying on the judgement of Supreme Court in the case of Engineering Analysis. The DRP did, however, classify AMC charges as FTS/FIS under Article 12(4)(b) of the India-USA DTAA basis the argument that the support services were specific and exclusive to the taxpayer's products and significant technical expertise was involved in such services. The DRP also observed that the training provided by the assessee allowed the user to acquire / develop the capability to independently use the products and hence made available technical knowledge to the user.

The ITAT held that the taxpayer supplied software to RJIL on a non-transferable, non-exclusive basis, granting only the right to use the software and what was supplied was a copyrighted article and not a copyright in the software. Relying on the Supreme Court's ruling in Engineering Analysis, it held that in the absence of permanent establishment, supply of software license was not taxable in India in terms of India-USA DTAA.

Further, the ITAT observed that the Service Level Agreement which included AMC services was a part of the Software License Agreement and hence the services provided to RJIL were ancillary and subsidiary to the licensing of software and would therefore be characterised in the same manner as that of the predominant/ original transaction which was the supply of Software. Additionally, the test of "make available" under article 12(4)(b) of the India-USA DTAA would not be satisfied since imparting training or educating a person with respect to functionality and attributes of a software or application would clearly not amount to the rendering of technical service. It accordingly held that AMC services rendered by the taxpayer were not liable to tax in India.

The ITAT reiterates the understanding that AMC charges should be characterized in the same manner as the predominant transaction. This interpretation aligns with the commercial understanding of such agreements, wherein maintenance and support services are typically bundled with software licenses to ensure their proper functioning over time. Consequently, the ruling provides clarity on the tax treatment of AMC charges under international tax treaties, ensuring that they are not subjected to taxation as FTS.

UK LLP, a fiscally transparent entity, entitled to treaty benefits for pre-protocol amendment years

Herbert Smith Free LLP [ITA No. 3994/Del/2017 - Order dated 8 April 2024 (Delhi ITAT)]

Taxpayer, a UK based LLP is a firm of Solicitors registered in UK with majority of its partners being tax residents of UK. It rendered legal services to its clients situated in India/outside India relating to activities carried out by such clients in India. AO argued that an LLP is not taxable in UK in its capacity as an LLP, it is the partners of the LLP in UK which are taxable. Accordingly, AO held that LLP being a fiscally

Important Rulings

transparent entity (FTE) would not fall within the purview of a resident within the meaning of Article 4(1) of the India-UK DTAA and therefore would not be eligible for benefit of India-UK DTAA. The CIT(A) upheld the order of the AO and further observed that the Protocol which amended the treaty w.e.f. 27.12.2013 and included partnership firms (FTEs) within ambit of Article 4 was prospective and hence the position prior to the amendment was that a fiscally transparent partnership firm was not liable to tax and could not be a resident for the purpose of the DTAA.

The taxpayer contended that it should qualify for DTAA benefits, citing that the LLP is treated as a body corporate under the UK law and its income is taxed in the UK through its partners. The taxpayer referenced various judicial precedents, including Mumbai Tribunal ruling in the case of Linklaters LLP and Calcutta High Court ruling in the case of P & O Nedlloyd Ltd. & Ors. etc., wherein judicial authorities had granted treaty benefits to similar entities holding that as long as the entire income of the partnership firms were taxed in the residence country, regardless of whether the tax was levied on the entity or its partners, treaty benefits could not be denied.

The ITAT noted that the taxpayer's case was squarely covered by the Mumbai Tribunal decision of Linklaters LLP, wherein it was held that the taxpayer was entitled to the benefit of India-UK DTAA on the portion of its income from Indian engagements, which had been taxed in UK in the hands of its UK tax resident partners. The ITAT clarified that in order to determine the eligibility of claiming the DTAA benefits, what is relevant is that the entity person should be taxed in its resident jurisdiction (i.e., fact of taxability) and not necessarily that the tax liability should actually be imposed and discharged by the same entity person (i.e., mode of taxability). The ITAT further accepted the taxpayer's contention that the favourable judgements rendered by judiciary pertained to pre-protocol amendment years and were pronounced after the protocol amendment came into effect and hence the revenue's argument that the said judgements were rendered without considering the implication of the protocol amendment could not be accepted.

Legal & Professional Services for product registration not taxable as no technology made available

Cadila Pharmaceuticals Ltd [ITA Nos. 51 & 52 and 73 & 76 /Ahmedabad/2020 – Order dated 17 April 2024 (Ahmedabad ITAT)]

Taxpayer had obtained legal and professional services from non-residents in respect of registration of its products with the foreign regulatory authorities for sales in those countries. The taxpayer had contended that in view of the sub-clause (b) of section 9(1)(vii) of the Act, the amount payable by the resident to non-resident towards fees for technical services was not taxable in India, if the said services were availed for earning income from any source outside India. The taxpayer had further contended that such services availed by the taxpayer did not 'make available' any technical knowledge, skills, or knowhow to it and therefore, the said services did not constitute FTS as per the India-US DTAA.

The ITAT noted that the services did not involve any transfer of technical knowledge, skill, or know-how etc. and the services rendered did not make available any technical knowledge,

Important Rulings

skill, or know-how etc. to the taxpayer. The department being unable to controvert the above findings, the matter was decided in favour of the taxpayer.

ITAT confirms India-Cyprus DTAA benefits, recognizes Taxpayer as "Beneficial Owner"

Little Fairy Ltd [ITA No. 1513/Del/2022 – Order dated 15 May 2024 (Delhi ITAT)]

Taxpayer, incorporated and tax resident of Cyprus, is a wholly owned subsidiary of IL&FS India Realty Fund II LLC, a Mauritius based entity. Taxpayer subscribed to the compulsorily convertible debentures (CCDs) of India Bulls Infra Estate Limited (Indian Company) and earned the interest income which was offered to tax in India at concessional rate of 10% in terms of Article 11 of India Cyprus DTAA.

The Revenue denied the benefit of DTAA by observing that taxpayer was not the beneficial owner of the interest income as it did not carry out any active business activities in Cyprus, had hardly any presence in Cyprus, and was merely a conduit for channelizing the interest funds and accordingly, AO taxed the income at 40% under the Income-tax Act, 1961.

Rejecting the contentions of the Revenue, ITAT allowed the appeal, based on following findings:

- Taxpayer had furnished the tax residency certificate (TRC).
- Taxpayer had right to receive and enjoy the interest income earned on CCDs without any obligation to pass to any other person.
- All the Board meetings were held in Cyprus where the decisions related to its operations were taken independently.
- Taxpayer being an investment company, there was no need to undertake any business activity like manufacturing or trading concern and did not require any personnel other than directors in its payroll who were well qualified and competent to take business investment decisions.
- Taxpayer had availed the services of professional administrator for its day-to-day administration in Cyprus.

The ITAT further observed the well settled principle that shareholders and company are distinct and separate from each other and the shareholders being beneficial owner of the shares of a company do not get any beneficial ownership over the assets of the company.

The subject of Beneficial Owner has always been debatable, particularly when the jurisdictions involved are Mauritius, Cyprus, and Singapore. This is despite the Circular 789 dated 13th April 2000 clarifying that TRC will constitute sufficient evidence for the purpose of residential status and plethora of judicial precedents. The issue of whether TRC is conclusive to claim the DTAA benefits from a tax residency and beneficial owner (in the context of capital gain) standpoint is currently pending before the Supreme Court (SC) in the case of Blackstone Capital Partners (Singapore) VI FDI Three Pte. Ltd. [2024] 159 taxmann.com 389 (SC) and matter is listed for hearing in September 2024.

Important Rulings

Foreign Ruling

ORAs treated as Equity; Issuance Costs non-deductible against PE Profits under Netherlands-France DTAA

[X] S.E. vs. The State Secretary for Finance [21/00415 - Order dated 17 May 2024] (Supreme Court of the Netherlands)]

The taxpayer, a company incorporated under the domestic laws of France engaged in renting of real estate had a PE in Netherlands. The assets of the PE included shares of a company resident of Netherlands ('NL NV') which the taxpayer had acquired by means of exchange offer. As per the exchange offer, the taxpayer issued new shares and convertible bonds (ORAs) against the shares of NL NV. The shareholders of NL NV could opt for the ORAs or new shares.

The taxpayer had incurred cost with respect to issuance of ORAs and new shares and the same was claimed as a deduction against the profits attributed to the PE in Netherlands. The said position of the taxpayer was not accepted by the Tax Inspector and consequently, taxpayer filed an appeal before the Amsterdam Court of Appeal.

The said matter majorly involved the following issues:

- Whether the ORAs be characterized as debt or equity, and
- Whether deduction with respect to issue cost for ORAs and new shares be allowed to be charged against the attributable profits of the PE

The Amsterdam Court of Appeal with respect to characterization of ORAs held that the most essential element of the commitment between the ORAs and the taxpayer was the right of the ORAs holders to redeem the ORAs in the form of shares. This might pose a risk to the ORAs holders of receiving less than the nominal value of the ORAs when shares were issued against the ORAs. Further, the court observed that there was no enforceable obligation to repay the ORAs and accordingly held that ORAs could not be regarded as debt capital.

The Supreme Court of Netherlands observed that for a provision of money to be regarded as a loan there must exist an obligation to repay under the civil law. The exchange offer entered between NL NV and taxpayer did not give ORAs holders an enforceable right for repayment in cash, but only an enforceable right for repayment in shares. It, accordingly, upheld the order of the Court of Appeal and held that ORAs did not constitute debt instruments.

Further with respect to allowability of deduction towards issuing costs, the Court of Appeal held that the issuing costs must be regarded as organ costs which could not be linked to certain benefits obtained by the person concerned even if they were obtained with or from the permanent establishment. Further, pursuant to analyzing Netherlands - France Tax Convention, the Court of Appeal concluded that it could not be inferred either from the DTAA or from commentary of OECD Model Tax Convention that cost with respect to issue of ORAs were attributable to PE in the Netherlands or that they must be regarded as costs within the meaning of Article 7 of Netherlands France DTAA. Hence, it held that the said costs were not allowable as deduction against the attributable profit of the PE in the Netherlands. The Supreme Court upheld the order of Court of Appeal and held that without prejudice to the characterization of ORAs, the issuing costs did not depend on the way in which the capital would be used. Such

Important Rulings

costs were inherent in the legal form of a company with capital divided into shares and could not be linked to its PE.

It is important to note that the said ruling characterized the ORAs instruments as "Equity" under the local civil law and tax laws, notwithstanding the fact that claim of the ORAs holders took precedence over claims by the shareholders. It underscores the importance of understanding local civil law's implications on tax matters. Various interesting issues like whether the ORAs holders to be treated at par with shareholders, whether interest earned on the said ORAs will amount to dividend income, whether ORAs be considered as equity from the outset thereby impacting the deductibility of related expenses and interest etc. have been untouched in the said ruling.

Important Updates

Foreign Updates

UAE FTA issues Corporate Tax Guide on Business Restructuring Relief

In its ongoing commitment to supporting corporate taxpayers in comprehending and navigating the complexities of the UAE's corporate tax framework, the Federal Tax Authority (FTA) has published the Business Restructuring Relief Guide for Corporate Tax Purposes. This guide is intended to offer detailed guidance on the Business Restructuring Relief provisions outlined in Article 27 of the UAE Corporate Tax Law.

Article 27 of the UAE Corporate Tax Law addresses Business Restructuring Relief, providing tax relief for companies undergoing reorganizations such as mergers and acquisitions. It sets out conditions for eligibility, types of qualifying transactions and the tax implications, circumstances when the relief will be clawed back and the consequences of claw back of the relief. This provision aims to facilitate corporate efficiency and economic growth by easing the tax burden during restructuring.

The guide provides detailed insights into the types of transactions eligible for this relief, along with illustrative examples to enhance understanding. However, it is essential to recognize that unlike tax laws, these guidelines are not legally binding.

IRBM publishes Revised Tax Guidelines on Gains from Disposal of Foreign Capital Assets

The Inland Revenue Board of Malaysia (IRBM) has released updated guidelines on the tax treatment on gains from the disposal of foreign capital assets received in Malaysia by a resident. Initially published on March 27, 2024, these guidelines were revised on April 26, 2024.

The guidelines provide clarity on compliance, documentation, and reporting standards necessary to support tax exemption claims, ensuring alignment with IRBM regulations.

The revisions focus on the tax exemption for gains from foreign capital assets brought into Malaysia between 2024 to 2026. To qualify for the exemption, taxpayers must meet specific economic substance requirements, demonstrating genuine economic activity related to the assets.

Administrative Measures for management of Beneficial Owner Information

In order to enhance market transparency, maintain order, and prevent money laundering and terrorist financing, the People's Bank of China, and the

Important Rulings

State Administration for Market Regulation (SAMR) has jointly introduced new measures on beneficial owner information effective from November 1, 2024. This regulatory step is part of broader efforts to align with international standards on anti-money laundering and financial transparency.

These measures require some prescribed entities to register beneficial owner information.

Exemptions to the above apply to individual industrial and commercial households and entities with capital contributions not exceeding 10 million Chinese Yuan, provided all shareholders and partners are natural persons and various conditions are adhered with.

The beneficial owner refers to the natural person who ultimately owns or actually controls the reporting entity or enjoys its ultimate benefits. A natural person is the beneficial owner of a reporting entity if he/she meets one of the following criteria:

- A natural person who, directly or indirectly, ultimately owns more than 25 percent of the equity, shares or partnership interests of the reporting entity.
- A natural person who does not meet Criterion 1 but is ultimately entitled to more than 25 percent of the income and voting power of the reporting entity.
- A natural person who does not meet Criterion 1 but individually or jointly exercises de facto control over the reporting entity.

ATO issues Taxpayer Obligations for Withholding Tax on Payments to Non-Residents

The Australian Taxation Office (ATO) recently issued a notice outlining obligations for taxpayers who have made interest, dividends, or royalty payments subject to withholding tax to non-residents.

Taxpayers who have paid interest, dividends, or royalties subject to withholding tax, to a non-resident, have an obligation to:

- Lodge a Pay as you go (PAYG) withholding from interest, dividend, and royalty payments to non-residents - annual report by 31 October each year and/or
- Lodge an annual investment income report by 31 October each year, if you are an investment body making interest payments to non-resident investors (or lodge a nil return), and
- Pay withholding tax to the ATO, unless a withholding exemption or tax treaty relief applies.

In addition to outlining taxpayer obligations, the ATO highlighted specific areas of focus for scrutiny. These include situations where entities defer interest to avoid or delay withholding tax while still claiming income tax deductions on an accrual basis. Furthermore, the ATO will closely monitor cases involving offshore-related entities attempting to evade withholding tax on interest expenses deducted from Australian-sourced income and paid to non-residents.

Streamlining Transfer Pricing: Malaysia's Updated APA Application Process

An advance pricing arrangement (APA) is an arrangement between a taxpayer and the Director General of Inland Revenue (DGIR) or between Competent Authorities that determines the transfer pricing methodology to ascertain the prospective arm's length transfer prices of specified related party transactions between the taxpayer and its foreign affiliates over a specified period of time, under specified terms and

Important Rulings

conditions. There are three types of APA, namely Unilateral APA ("UAPA"), Bilateral APA ("BAPA") and Multilateral APA ("MAPA")

The Ministry of Finance in Malaysia released two new rules governing transfer pricing (TP) norms in the country: the Income Tax (Advanced Pricing Arrangement) Rules 2023 and the Income Tax (Transfer Pricing) Rules 2023. Additionally Advance Pricing Arrangement Guidelines were released in 2024 explaining the manner in which taxpayer may apply for APA.

The Inland Revenue Board of Malaysia updated its APA webpage, where the related forms for the submission of APA application are enabled, including:

A. Unilateral Advance Pricing Arrangement Form
B. Bilateral Advance Pricing Arrangement Form

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Important Rulings

Assessing Officer is obliged to pass draft assessment order under section 144C(1) even in partial remand proceedings

ExxonMobil Company India (P.) Ltd. vs. DCIT [Bombay High Court] [2024] 162 taxmann.com 93 (Bombay)

During the year under consideration, the taxpayer had entered into international transaction of rendering technical services and back-office support services. Taxpayer's case was selected for scrutiny assessment and was referred to the Transfer Pricing Officer (TPO).After incorporating the recommended transfer pricing adjustments mentioned in the TP Order and other disallowances, the AO passed a draft assessment order under section 144C, against which no action was taken by the taxpayer and accordingly the AO finalized the assessment order.

The taxpayer filed an appeal against the same with CIT(A). CIT(A) upheld the transfer pricing additions and part of other disallowances. Against the said order of CIT(A), taxpayer appealed to the Income Tax Appellate Tribunal (ITAT). The ITAT set aside the findings of the CIT(A) and AO and remanded the matter back to the file of AO/TPO for fresh adjudication.

Pursuant to the ITAT's order, the AO referred the matter to TPO. The TPO issued the order recommending transfer pricing addition in relation to provision of back support services. The AO passed an order giving effect to the ITAT's order by making a transfer pricing addition. Aggrieved by the said order, the taxpayer filed a petition in High Court.

According to the taxpayer, the said order is barred by limitation as the ITAT order was passed on 27 July 2020 whereas the AO passed order on 30 January 2023 in case of remand proceedings. The taxpayer further argued that the AO was required to issue a draft assessment order before passing the final order, as mandated by Section 144C(1) even in remand back proceedings. Therefore, the order giving effect along with demand notice passed by AO was non-est in law and liable to be quashed.

The revenue contented that nowhere in the Act it is mentioned that provisions of Section 144C of the Act would be attracted while giving effect to the order of the ITAT. The draft order under section 144C of the Act had already been shared with taxpayer during the original assessment proceedings and just because the case was partially set aside by the ITAT for further verification on the issue of transfer pricing adjustment does not mean that the draft assessment order under Section 254 read with Section 144C (1) read with Section 143(3) of the Act was required to be passed.

Reliance was placed on the division bench of the court in the case of Dimension Data Asia Pacific PTE wherein it was held that even in partial remand proceedings from the Tribunal, the AO is obliged to pass a draft assessment order under section 144C(1) of the Act. Further, the "fresh adjudication" itself would imply that it would be an order which would decide the dispute between the parties which have been restored back to the AO.

Therefore applying the aforesaid principles to the facts of this case, it was held by the High Court that the failure on the part of the AO to follow the procedure under Section 144C(1) is not a merely procedural or inadvertent error, but a breach of a mandatory provision. Thus, it was clear case of jurisdictional error.

Important Rulings

Accordingly, the order passed by AO was required to be quashed and set aside as void ab initio.

Consequently, it may be inferred that the AO is obliged to pass draft assessment order in case of eligible tax payers for assessment and adjudication even in case of partial remand back proceedings in terms of Section 144C of the Act. Failure to do so will deprive the taxpayers of their valuable right to raise objections against such draft order before DRP which would be denial of substantive rights to the taxpayer and accordingly the final order passed by AO with passing draft order may be considered as voib ab initio. It may be noted that a different view is also taken by Madras High Court in case of similar issue.

Segregation of the milk from the water is necessary for ALP determination / Actual length of the controlled connection to be considered for the determination of ALP

Key Point Technologies (India) Private Limited [TS-190-ITAT-2024(HYD)-TP]

The taxpayer is engaged in the development of mobile application software and user interface technology for its customers including its Associated Enterprise i.e., Keypoint Technologies (UK) Limited ('Keypoint UK). The taxpayer had entered into a software development agreement dated September 01, 2015, for providing the software development services to its AE i.e., Key point UK.

For the purpose of computing the arm's length price of the services provided to its AE, the case of the taxpayer was referred to the transfer pricing officer ('TPO'). The TPO made an adjustment to the software development income by considering the whole year i.e., from April 1, 2015 to March 31, 2016 instead of the actual date of entering into the agreement i.e., Sept 01, 2015. The decision of the TPO was also upheld by the Dispute Resolution Panel ('DRP'). Aggrieved by the decision of the TPO and DRP, the taxpayer made an appeal before the Hyderabad Income Tax Tribunal (Hyderabad ITAT).

The Hyderabad ITAT took cognizance of the actual date of the agreement entered into by the taxpayer with its AE, which was also explicitly brought about in the TP documentation by the taxpayer. The Hyderabad ITAT remitted the matter back to TPO stating to verify the actual date of agreement, post which if found true, the adjustment shall be restricted to the actual period of agreement i.e., from Sept 01, 2016 to March 31, 2016 instead of the whole year.

Points to ponder for the reader:

Although the circumstances surrounding the transaction are not explicitly mentioned in the ITAT order, but it seems from the judgement that the transaction between the taxpayer and the other party came into the purview of the Chapter X post the signing of the agreement and the services if any provided by the taxpayer to Key point UK prior to the entering into the agreement were not influenced by the special relationship between taxpayer and AE, if any. *In this regard, it is important to note that the definition of AE is triggered if the conditions of section 92A are met at ANY point of time during the previous year. It becomes apparent on part of the taxpayer to substantiate that the transactions entered, if any, prior to the existence of the AE relationship or any agreement in place have not been subjected to any influence arising out of the AE relationship.*

Important Rulings

Netting off of outstanding balances prohibited on an entity level basis / Netting off of outstanding balances shall be carried out qua AE

Rockwell Automation India Pvt Ltd [TS-195-ITAT-2024(DEL)-TP]

The taxpayer is engaged in design, manufacturing, install, repair, and deals in industrial, electrical, and electronic products. The taxpayer had entered into a plethora of international transactions resulting into various amounts of payables and receivables that had remained outstanding for prolonged period of time. The TPO identified the outstanding receivables and, noting that the taxpayer had not provided invoice-wise details, proceeded to impute interest at a rate of LIBOR plus 400 b.p. on the outstanding receivables for a period of 182 days.

Aggrieved by the TPO's order, taxpayer appealed to the DRP, arguing that there were also significant payable outstanding to its AEs on which no interest was being paid by the taxpayer himself and accordingly, ought to be netted of against the receivables. The DRP accepted this argument and directed the TPO to recompute the interest chargeable on the net outstanding receivables, which led to a reduction in the adjustment owning to the interest chargeable on the net outstanding receivable.

Again, aggrieved by the DRP's order, the taxpayer filed an appeal before the Delhi ITAT. The taxpayer alleged that it had outstanding receivables and payables from multiple AEs spanning across varied regions / countries and accordingly, all the outstanding balances ought to be netted off on an aggregate basis. The Delhi ITAT rejected the contention of the taxpayer and held that the netting off cannot be carried out on an entity level but shall be done qua respective AEs.

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RBI Notifications

Fair Practices Code for Lenders – Charging of Interest

RBI / 2024 – 25 / 30 issued vide DoS. CO. PPG. SEC. 1 / 11. 01. 005 / 2024 - 25 dated April 29, 2024

RBI has been giving guidelines on Fair Practices to Regulated Entities (REs) on the fairness and transparency in charging interest while at the same time providing ample freedom for REs to decide on the loan pricing.

In recent past it has come to the notice of Reserve Bank of India (RBI) that several lenders are resorting to certain unfair practices in charging interest, some of which are stated below:

a) Charging of interest from the date of sanction of loan or execution of loan agreement instead of charging interest from the date of actual disbursement of funds to customers.
b) Charging of interest from the date of issuance of cheque, even if the cheque was handed to the customer several days later, in cases where loans were disbursed by cheque.
c) Charging interest for the entire month, in place of charging the same for part of the month, even if disbursal or repayment occurred during the month.
d) REs was collecting one or more instalments in advance but charging interest on the full loan amount.

RBI has directed REs to review their practices regarding mode of disbursal of loans, application of interest and other charges and take corrective action, wherever required. RBI has also advised REs to refund any excess interest and other charges levied to customers.

Effective date: Immediate effect

Risk Management and Inter-Bank Dealings: Amendments

RBI / 2024 – 25 / 32 issued vide A. P. (DIR Series) Circular No. 04 dated May 03, 2024

Reserve Bank of India has made certain amendments to the provisions governing foreign exchange derivative contracts, including Standalone Primary Dealers (SPDs) who had been granted permission from 2018 to provide forex products to its Foreign Portfolio Investor (FPI) clients. The primary amendments made vide this Circular are enumerated below:

1. Authorized Persons shall include Authorized Dealer Category - I banks, Standalone Primary Dealers authorized as Authorized Dealer Category – III and for the purpose of exchange traded currency derivatives, Recognized Stock Exchanges and Recognized Clearing Corporations, authorized under Section 10 (1) of the FEMA, 1999.
2. Standalone Primary Dealers may borrow foreign currency from their parent or correspondent outside India or any other entity, provided they adjust their overdraft within five days.
3. Stipulated time period for reporting obligations on part of Authorized dealers has been revised to 30th of the month following the end of the quarter.
4. Timelines for reporting to the Trade Repository of Clearing Corporation of India Ltd. (CCIL) has been formalized.

These amendments and revisions shall align the permitted foreign exchange derivative contracts including ETCD products provided by Authorized

RBI Notifications

Dealer Category – I Banks and the Standalone Primary Dealers as well as reporting compliances undertaken by these entities.

Effective date: Immediate effect

Margin for Derivative Contracts

RBI / 2024 – 25 / 34 issued vide A. P. (DIR Series) Circular No. 05 dated May 08, 2024

Based on market feedback, the RBI has superseded the Foreign Exchange Management (Margin for Derivative Contracts) Regulations, 2020 with the Reserve Bank of India (Margin for Derivative Contracts) Directions, 2024 vide notification no. FEMA.399(1)/2024-RB dated April 30, 2024. Some of the salient features of the new Directions are as follows:

A. **Authorized Dealers may Post and Collect Margin,** in India and outside India,
    - For a permitted derivative contract entered with a person resident outside India and receive as well as pay interest on such margin;
    - For derivative transactions of their overseas branches and IFSC Banking Units and receive and pay interest on such margin;
    - AD Cat-I banks may post and collect margin on behalf of their customers for a permitted derivative contract entered into with a person resident outside India and receive / pay interest on margin.

B. **Form of Margin posted and collected in India -** May be in the form of:
    - Freely convertible foreign currency and;
    - Debt securities issued by foreign sovereigns with a credit rating of AA- and above.

Effective date: Immediate effect

Master Direction – Reserve Bank of India (Margining for Non-Centrally Cleared OTC Derivatives) Directions, 2024

RBI vide Notification No. RBI / FMRD / 2024 – 25 / 117 / FMRD. DIRD. 01 / 14. 01. 023 / 2024 – 25 dated May 08,2024

The Master Direction – Reserve Bank of India (Margining for Non-Centrally Cleared OTC Derivatives) Directions, 2024 supersede the Master Direction - Reserve Bank of India (Variation Margin) Directions, 2022 dated June 01,2022.

Central counterparty means an entity that interposes itself between counterparties to contracts traded in one or more financial markets, becoming the buyer to every seller and the seller to every buyer and thereby ensuring the performance of open contracts.

A central counterparty (CCP) is a clearing house which becomes a counterparty to trades with market participants through novation, an open offer system, or another legally binding arrangement. For the purposes of the capital framework, a CCP is a financial institution including the following, namely

- Clearing Corporation of India (CCIL)
- Indian Clearing Corporation Ltd (ICCL)
- NSE Clearing Ltd (NSCCL)
- Multi Commodity Exchange Clearing (MCXCCL)
- India International Clearing Corporation (IFSC) Ltd (IICC) and
- NSE IFSC Clearing Corporation Ltd (NICCL).

The provisions of these Directions are applicable to Non-Centrally cleared foreign exchange derivative contracts, non-centrally cleared

RBI Notifications

interest rate derivative contracts, non-centrally cleared credit derivative contracts or any other non-centrally cleared derivative contract.

The Master Direction gives guidelines on the types of entities covered, the margins (both variation and initial margin), the working formula for calculation of margins, the methodology for exchange of margin, requirements and types of collateral for margining purposes along with margining compliances in overseas jurisdiction.

Effective Date: November 08, 2024

Issuance of partly paid units to persons resident outside India by investment vehicles under Foreign Exchange Management (Non-debt Instruments) Rules, 2019

RBI / 2024 – 25 / 36 issued vide A.P. (DIR Series) Circular No.07 dated May 21, 2024

Foreign Exchange Management (Non-debt Instruments) (Second Amendment) Rules, 2024 vide S.O. 1361(E), dated March 14, 2024, enabled issuance of partly paid units to persons resident outside India by Investment vehicles.

Consequently, partly paid units issued by Alternative Investment Funds (AIFs) to Persons resident outside India prior to the aforesaid amendment in March 2024 can now be compounded subject to regularising such issuances by taking the necessary administrative actions including reporting of issue of party paid shares on the FIRMS Portal.

Launch of PRAVAAH, RBI Retail Direct Mobile Application and FinTech Repository

Press Release: 2024-2025/393 dated May 28, 2024

RBI has launched three major initiatives:

1. **PRAVAAH Platform for Regulatory Application, VAlidation and AutHorisation) portal:**

   It is a secure and centralized web-based portal for any individual or entity to seek authorization, license or regulatory approval on any reference made by it to the Reserve Bank.

   At Present, 60 application forms covering different regulatory and supervisory departments of RBI have been made available on the portal.

2. **Mobile Application for RBI Retail Direct portal:**

   The retail direct portal was launched in November 2021 to facilitate retail investors to buy G-Secs in the primary auctions as well as buy and sell G-Secs in the secondary market. The launch of the **retail direct mobile app** will allow retail investors to transact in G-Secs through the mobile app on their smartphones.

3. **FinTech Repository:**

   FinTech Repository has been prepared by the RBI to capture essential information about FinTech entities, their activities, technology uses, etc. whether such entities are regulated or unregulated which can be accessed by https://fintechrepository.rbihub.in.

   Another repository for RBI regulated entities (banks and NBFCs) on their adoption of emerging technologies (like AI, ML, Cloud Computing, DLT, Quantum, etc.) called EmTech Repository has also been launched which can be accessed through https://emtechrepository.rbihub.in.

   The FinTech and EmTech Repositories are secure web-based applications and are managed by the Reserve Bank Innovation Hub (RBIH), a wholly owned subsidiary of RBI.

SEBI Notifications

Flexibility to Alternative Investment Funds (AIFs) and their investors to deal with unliquidated investments of their schemes

SEBI / HO / AFD / PoD – I / P / CIR / 2024 / 026 dated April 26, 2024

SEBI (Alternative Investment Funds) (Second Amendment) Regulations, 2024, were notified to provide greater flexibility to Alternative Investment Funds ("AIFs") and investors to deal with unliquidated investments of their schemes.

Regulation 2(1)(ia) of AIF Regulations states the definition of "*Dissolution period*" which has to be read in conjunction with 2 (1)(pb) of the aforesaid Regulations which defines the "*Liquidation period*" –

"*Dissolution period*" means the period following the expiry of the liquidation period of the scheme for the purpose of liquidating the unliquidated investments of the scheme of the Alternative Investment Fund.

"*Liquidation period*" means a period of one year following the expiry of tenure or extended tenure of the scheme of an Alternative Investment Fund.

A. Dissolution Period:

As per Regulation 29(9), during the liquidation period an AIF may enter into the dissolution period after obtaining approval of at least seventy five percent of the investors by value of their investment in the Scheme.

In this regard, the AIF / manager shall disclose the following to investors before seeking their consent.

- The proposed tenure of the dissolution period, details of unliquidated investments, value recognition of the unliquidated investments for reporting to Performance Benchmarking Agencies, etc.
- An indicative range of bid value, along with the valuation of the unliquidated investments carried out by two independent valuers.

The concept of dissolution period and the process thereof has been initiated to do away with some of the practical difficulties faced in the liquidation scheme framework laid out by SEBI by providing a more viable solution for AIFs to manage unliquidated investments.

B. Mandatory in-specie (other than cash) distribution of unliquidated investments

During Liquidation Period, if investor consent for dissolution or in-specie distribution isn't obtained

i. Unliquidated investments distributed in-specie without needing 75% investor consent.

ii. Value of distributed investments is recognized at one rupee for performance tracking.

iii. Investors' declining in-specie distribution results in write-off of their portion.

Applicability: With immediate effect

Nomination for Mutual Fund Unit Holders – exemption for jointly held folios

SEBI / HO / IMD / IMD – PoD – 1 / P / CIR / 2024 / 29 dated April 30, 2024

Master Circular No. SEBI/HO/IMD/IMD-PoD-1/P/CIR/2023/74 dated May 19, 2023, prescribes the requirement for nomination/opting out of nomination for all the existing individual unit holder(s) holding Mutual

SEBI Notifications

Fund units either solely or jointly, by June 30, 2024, failing which the folios shall be frozen for debits.

To streamline compliance and reduce costs, SEBI has decided that the requirement of nomination shall be optional for jointly held Mutual Fund folios.

[Note: SEBI vide Circular No. SEBI/HO/MIRSD/POD-1/P/CIR/2024/81 dated June 10, 2024, has put on hold the mandatory requirement of "choice of nomination" for demat accounts and mutual funds portfolios. The salient features of the circular are as follows:

For existing shareholders / unit holders:

- *Non-submission of 'choice of nomination' shall not result in freezing of Demat Accounts as well as Mutual Fund Folios.*
- *Securityholders holding securities in physical form shall be eligible for receipt of any payment including dividend, interest or redemption payment and lodge grievance.*
- *Payments including dividend, interest or redemption payment withheld by the Listed Companies/RTAs, only for want of 'choice of nomination' will have to be released.*

For new shareholders / unit holders:

- *They shall be required to mandatorily provide the 'Choice of Nomination' for demat accounts / MF Folios (except for jointly held Demat Accounts and Mutual Fund Folios).*

Depositories and Depository Participants have been instructed to encourage the existing shareholders / unit holders to fill the "choice of nomination" by sending communication on email and SMS on a fortnightly basis as well as by way of pop-up messages whenever web / mobile application / platform of such DP is opened.]

Facilitating collective oversight of distributors for Portfolio Management Services (PMS) through APMI

SEBI / HO / IMD / IMD – PoD – 1 / P / CIR / 2024 / 32 dated May 02, 2024

Securities and Exchange Board of India vide its SEBI (Portfolio Managers) Regulations, 2020 stated that a Portfolio Manager has to ensure that any person or entity involved in the distribution of its services will have to carry out Portfolio Management Services (PMS) activities in compliance with the Regulations.

To ensure proper compliance with the guidelines set for Portfolio Management Services ("PMS") distributors at the industry level, SEBI has decided that any person or entity involved in the distribution of PMS will have to mandatorily obtain registration with Association of Portfolio Managers in India (APMI). Furthermore, Portfolio Managers have been directed to ensure that any person or entity engaged in the distribution of its services has obtained registration with APMI, in accordance with the criteria laid down by APMI.

Applicability: Effective from January 01, 2025 and APMI shall issue the criteria for registration of distributors by July 01, 2024.

SEBI Notifications

Portfolio Managers - Facilitating ease in digital on-boarding process for clients and enhancing transparency through disclosures

SEBI/HO/IMD/IMD-PoD-1/P/CIR/2024/35 dated May 02, 2024

To bring about ease in the digital onboarding of clients by the Portfolio Managers, the following measures have been prescribed by SEBI:

- A portfolio manager before taking up an assignment of management of funds and portfolio on behalf of a client now has to enter into an agreement with the client clearly defining the inter-se relationship and setting out their mutual rights, liabilities and obligations relating to management of portfolio.
- While onboarding clients, Portfolio Managers have to ensure that:
  a) The client has understood the structure of fees and charges.
  b) The new client has separately signed the annexure on fees and charges and understood the structure of fees and charges.
- Portfolio Manager also have to provide a fee calculation tool to all their clients that highlights various fee options with multi-year fee calculations. Such tool shall incorporate the high watermark principle, wherever applicable.
- To easily understand the critical aspects of the Portfolio Manager-client relationship, Portfolio Manager also has to provide "Most Important Terms and Conditions (MITC)" document to its clients, which has to be duly acknowledged by the client.

Applicability: Effective from October 01, 2024

Periodic reporting format for Investment Advisers

SEBI / HO / MIRSD / MIRSD – PoD – 2 / P / CIR / 2024 / 38 dated May 07, 2024

Investment Advisers Administration and Supervisory Body ("IAASB") has been set up with the purpose of administration and supervision of Investment Advisers ("IAs") in line with Regulation 14 of the Investment Advisors ("IA") Regulations. Given the fact that current reporting requirements specified by the IAASB are ad-hoc, SEBI has proposed a standardization of periodic reporting by the IAs.

For guidance on standardization of reporting formats and timelines for reporting, SEBI has considered the recommendations of Industry Standards Forum ("ISF") for IAs and provided both reporting formats as well as timelines for submissions.

Applicability: With immediate effect

Timelines for submission of periodic reports to IAASB:	
For the half-yearly period ending on March 31, 2024	within a period of fifteen days from the date of issuance of circular
For the subsequent half-yearly periods	Within seven working days from the end of the half-yearly period

Certification requirement for key investment team of manager of AIF

SEBI Notifications

SEBI/HO/AFD-1/AFD-1-PoD/P/CIR/2024/42 dated May 13, 2024

To ensure proper functioning of the Alternative Investment Funds ("AIFs"), SEBI had mandated that at least one key personnel from the investment team or the Manager of the Alternative Investment Fund, should obtain certification from the National Institute of Securities Market ("NISM") by clearing the NISM Series-XIX-C: Alternative Investment Fund Managers Certification Examination. NISM a public trust established by SEBI for the purpose of carrying out a wide range of capacity building activities aimed at enhancing quality standards in the securities markets.

Conditions / timelines specified for such registration with NISM stated herewith:

1. The criterion NISM certification shall form the basic eligibility criteria for all applications seeking registration of AIFs and launch of any schemes by AIFs on or after May 10, 2024 – New Schemes.
2. Existing schemes of AIFs and those with pending applications with SEBI as on May 10, 2024, will comply with the registration requirements on or before May 09, 2025 – Existing Schemes.
3. The trustees or sponsors of the AIFs have to ensure that the Compliance Test Report prepared by the Manager includes compliance with the provisions of the aforesaid Circular.

Applicability: Immediate effect

Framework for considering unaffected price for transactions upon confirmation of market rumor

SEBI/HO/CFD/CFD-PoD-2/P/CIR/2024/51 dated May 21, 2024

To ensure that corporate actions such as pricing of further issue of shares / preferential allotment etc. are not affected / swayed by abnormal price fluctuations on account of market rumors, SEBI has issued framework for considering "unaffected price" so as to exclude such abnormal price disruptions while determining the price for such transactions.

LODR regulations has mandated that the top 100 listed entities are required to verify market rumors regarding a transaction, upon such material price movement. For ensuring that the unaffected price shall be considered for transactions on which pricing norms are mandated by SEBI, it is mandated that rumor pertaining to such transaction is reported within 24 hours from the trigger of such material price movement.

Further, it has been specified that the unaffected price shall be considered, by excluding the effect on the price of the equity shares of the listed entity due to the material price movement and confirmation of the rumor. Detailed Framework and guidelines for working the Volume Weighted Average Price ("VWAP") is specified in the Circular.

Applicability:

- Top 100 listed entities - from June 01, 2024
- Top 250 listed entities (i.e., next top 150) - from December 01, 2024.

Audiovisual (AV) presentation of disclosures made in Public Issue Offer Documents

SEBI/HO/CFD/CFD-TPD-1/P/CIR/2024/55 dated May 24, 2024

For ease in understanding the salient features of public issues by subscribers to the issue, SEBI

SEBI Notifications

vide this circular has mandated Audiovisual (AV) presentation to the investing public so as to avoid or rely on unauthorized/unsolicited information about public issues. The AV format will contain advisory to investors cautioning them not to rely on content from web, social media, micro blogging platforms including finfluencers and only to base their decision on information contained in the Offer document and Price Band Advertisement.

- AV presentation shall be prepared and placed in the public domain for all main board public issues.
- The presentation shall initially be in bilingual format i.e. English and Hindi will a content of around 10 minutes so as to capture the salient features of the issue.
- The contents of AV shall be as per the prescribed guidelines so as to ensure consistency in information sharing across public issues.

This approach aims to provide essential information in an easily understandable and accessible format, empowering investors with the knowledge needed to assess the risks and opportunities of public issues before investing. The Issuer and the Lead Managers to the Issue shall be responsible for the content and information provided in the AV.

Applicability:

- To all DRHP filed with SEBI:
- On or after July 01, 2024 - on Voluntary basis
- October 01, 2024 onwards - on Mandatory basis

Modification in Staggered Delivery Period in Commodity Futures Contracts

SEBI / HO / MRD / MRD – PoD – 1 / P / CIR / 2024 / 57 dated May 24, 2024

As per the Master Circular for Commodity Derivatives Segment notified vide SEBI/HO/MRD/MRD-PoD-1/P/CIR/2023/136 dated August 04, 2023:

"Staggered delivery period is the period, beginning few working days prior to expiry of any contract and ending with expiry, during which sellers/buyers having open position may submit an intention to give/take delivery."

Furthermore, all compulsory delivery commodity futures contracts (agriculture commodities as well as non-agriculture commodities) shall have a staggered delivery period.

SEBI has reduced the minimum duration of staggered delivery period to at least three working days from the existing, at least five working days from the date of expiry of contract. The rationale seems to be to provide additional time to buyers / sellers to square off their open positions before expiry instead of unwinding their existing trades at least five days before the date of expiry.

Applicability:

Effective from July 01, 2024, i.e., for contracts where staggered delivery is scheduled after this date.

MCA Notifications

Relaxation of additional fees and extension of last date of filing of Form LLP BEN-2 and LLP Form No. 4D under the Limited Liability Partnership Act, 2008

Ministry of Corporate Affairs ("MCA") has extended the last date of filing Form LLP BEN-2 and LLP Form No 4D, without payment of any further additional fees, up to July 01, 2024, to ensure better compliance by the reporting LLPs and keeping in view of transition of MCA-21 from version-2 to version-3.

Contributed by

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

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For further analysis and discussion, you may please reach out to us.

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Abbreviations

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

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

Abbreviation	Meaning
EPCG	Export Promotion Capital Goods
FEMA	Foreign Exchange Management Act, 1999
FII	Foreign Institutional Investor
FIFP	Foreign Investment Facilitation Portal
FIRMS	Foreign Investment Reporting and Management System
FLAIR	Foreign Liabilities and Assets Information Reporting
FPI	Foreign Portfolio Investor
FOCC	Foreign Owned and Controlled Company
FTC	Foreign Tax Credit
FTP	Foreign Trade Policy 2015-20
FTS	Fees for Technical Service
FY	Financial Year
GAAR	General Anti-Avoidance Rules
GDR	Global Depository Receipts
GMT	Global Minimum Tax
GILTI	Global Intangible Low-Taxed Income
GSTN	Goods and Services Tax Network
GVAT Act	Gujarat VAT Act, 2006
HSN	Harmonized System of Nomenclature
IBC	Insolvency and Bankruptcy Code, 2016

Abbreviations

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

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

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