

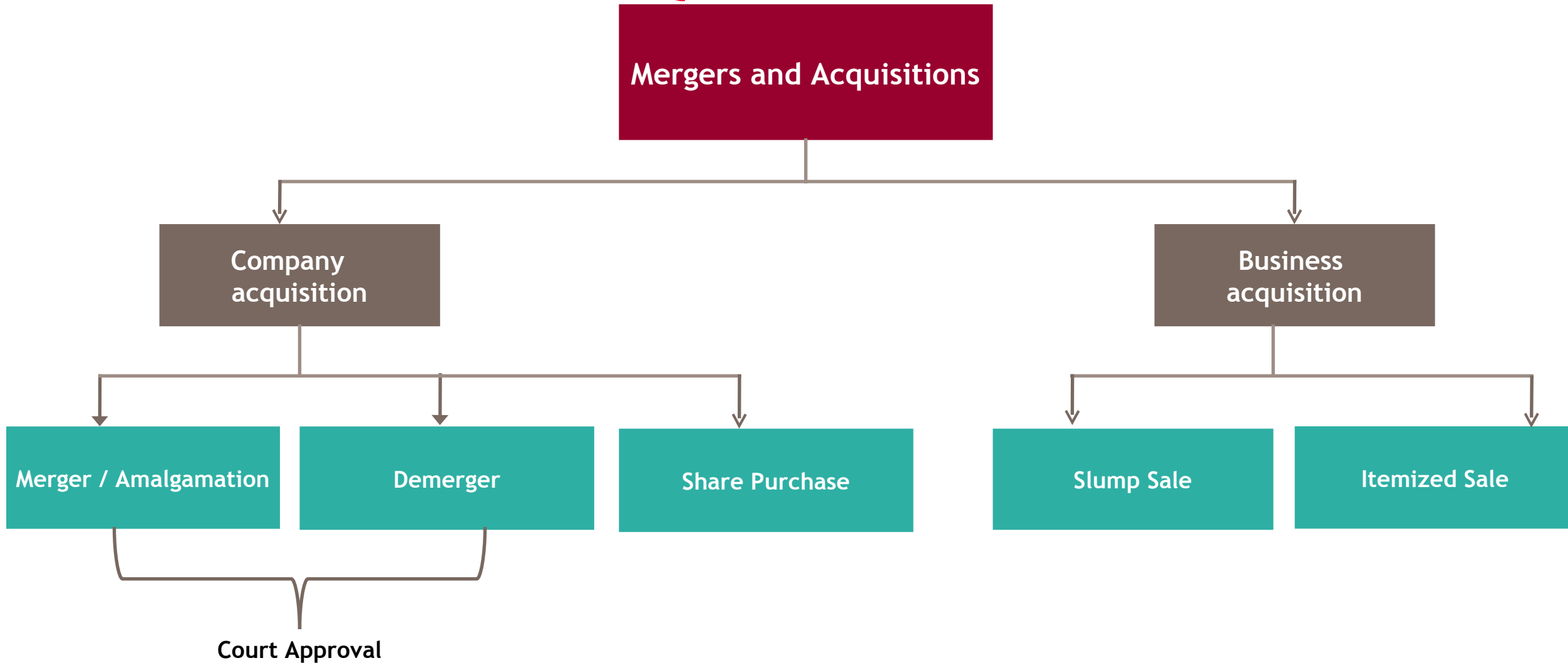
The background of the slide features two spotlights at the top, one on the left and one on the right, both casting bright beams of light onto a dark blue stage floor. The spotlights are recessed into the ceiling, and their beams create a soft glow on the floor below. The overall scene is dimly lit, with the spotlights providing the primary source of illumination.

Due Diligence - Indirect Tax

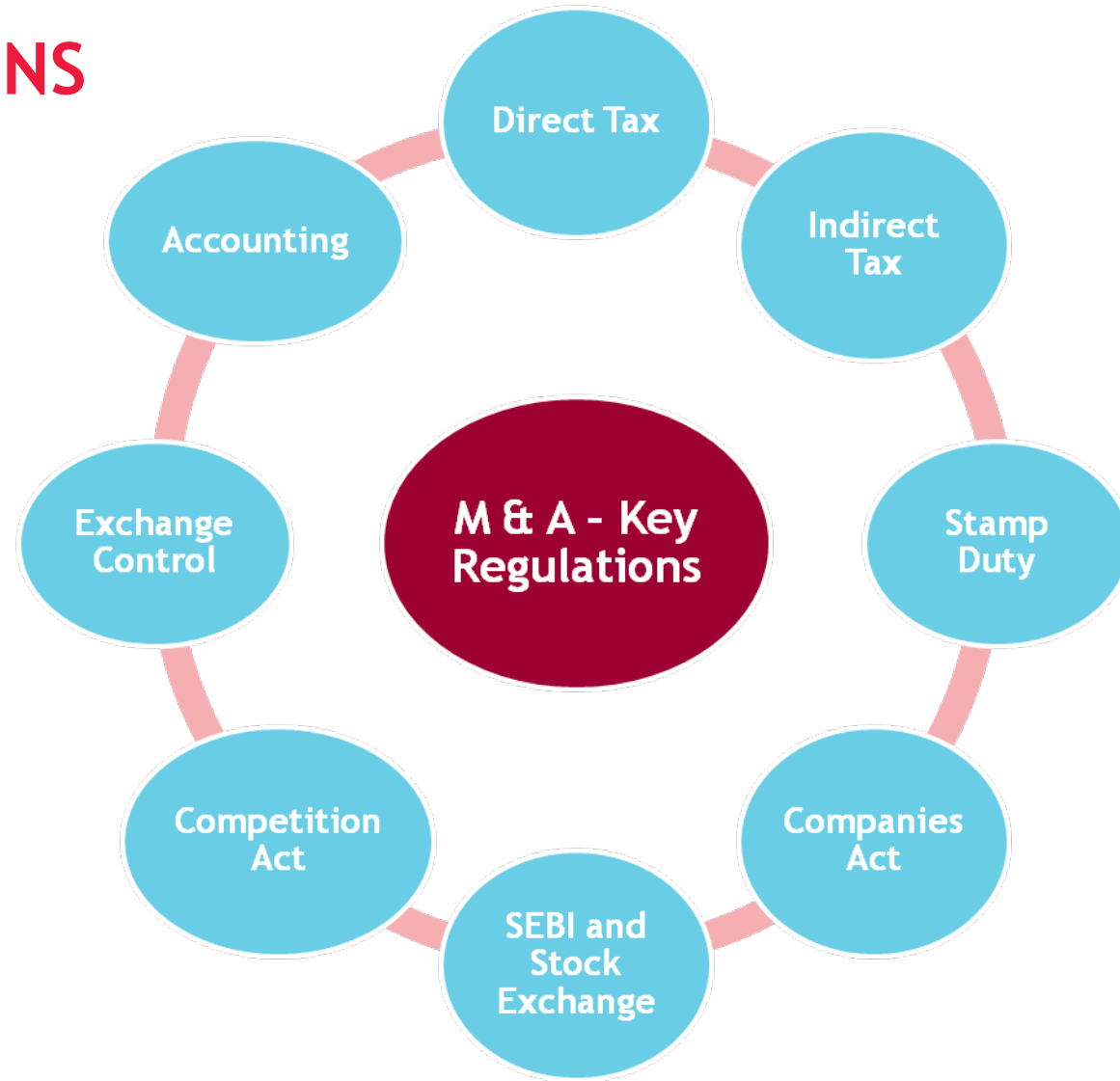
CA Yash Arya

Partner- Tax & Regulatory Services

MODES OF MERGERS AND ACQUISITIONS



KEY REGULATIONS



Contents

- Taxability of the transaction of business re-organization
- Fate of historical tax liabilities / tax assets (refunds etc.)
- Continuity of tax benefits, exemptions and obligations
- Transferability of tax credit balance
- Taxability of transaction during intervening period
- Procedural compliances (e.g. Change in Registration Certificates etc.)

Structuring of the transaction has bearing on taxability

Nature of transaction

- **Whether amalgamation / merger envisage transaction of extinction of shares in lieu of shares or money?**
 - Whether VAT applicable ? (Shares excluded from the definition of ‘Goods’)
 - Whether Service tax applicable? (Transaction of sale of business as ‘Going concern’ exempted)
- **Whether slump sale /de-merger involve transfer of business between two parties in return of money**
 - Whether VAT applicable? (No. since transfer of business as a whole and not individual assets. Business can not be termed as Goods)
 - Whether Service tax applicable ? (No, since transfer of business is covered under Negative List of services)
- **Sale of assets with values assigned to individual assets**
 - Movable assets transferred - Taxable as per provision of VAT/CST law
 - Immovable assets transferred - No VAT/CST. However, stamp duty is applicable

Slump Sale vs. sale of individual assets

Taxability of transactions - VAT & Service tax

- Sale of business and sale of goods are two different aspects.
- Business is not goods, hence transfer of business by slump sale or as going concern is not liable to VAT/CST
- *Judicial Pronouncements:*
 - Coromandal Fertilizers Limited vs. The State of A.P. [112-STC-1 A.P.]
 - Shri Ram Sahai vs. The Commissioner of Sales Tax [1963-14-STC-275-All]
 - Deputy Commissioner vs. K. Behnan Thomas [1977-39-STC-324-Mad]
- **Key points for consideration:**
 - Transfer of business is as a whole on going concern basis, including transfer of all assets and liability
 - Transfer is for a single/ lump sum consideration
 - Business Transfer Agreement does not provide any allocation of consideration to individuals assets transferred

Virtual transfer of assets and taxability

Implications of Central Excise and Cenvat Credit

Central Excise duty liability/ Reversal of CENVAT Credit

- Transfer of ownership is virtual transfer of goods outside the manufacturing premises, hence liable to Central Excise duty (Case)
- Transfer of ownership without movement of goods from the manufacturing premises, no liability to pay Central Excise duty (subject to dispute with Central Excise department)
- WIP and Finished goods - Central Excise duty liability
- Capital Goods and Inputs/ Raw material - reversal of CENVAT Credit (subject to depreciation allowance)

Transfer of business with tax liability - impact on valuation

Indirect Tax liabilities for historical transactions

- Transferee is responsible for all Indirect Tax liabilities even for past periods for ongoing business
- It's important to factor probability of tax liability for past transactions due to aggressive tax positions, insufficient documentation/ details, non receipt of statutory forms, pending WCT TDS certificates etc.
- The probable liability for past transactions has a bearing on the valuation of the business to be transferred
- Pending tax assessments- appropriate documents and details should be available and provided to the transferee
- Contingent liability and other enquiries/ notices from tax authorities to be disclosed, so as to factor the future tax liabilities in respect of past transactions.

Past transactions - Joint and several liability under MVAT

Liability in case of historic transactions

- Business Transfer - Merger/Amalgamation/De-merger/Slump sale:
 - As per Section 44(4) of the MVAT Act,
 - joint and several liability of tax, interest and penalty on the transferor and transferee and the person succeeding up to the time of such transfer, disposal or change.
 - In view of the above, the liability to pay historical VAT liabilities up to the date of transfer would be jointly and severally on the transferor and transferee
 - Joint and several liability would not apply in case of itemized sale of assets

Transfer of tax registrations

Liability for historical Transactions - Excise & Customs

- Business Transfer - Merger/Amalgamation/De-merger/Slump sale:
 - No specific provision under the Excise, Customs and Service tax laws for liability in case of transfer of business
 - Practically, in case of transfer of business requiring surrender of old registration and obtaining a new registration, the authorities typically insist on an undertaking from the buyer that he undertakes the liability to pay any tax, interest or penalty that may arise in future for past transactions
 - Right to re-course available: Right of attachment and sell extended to various articles which are in custody of transferee

Effective date of transfer of business

Intervening period transactions

- **Meaning**
 - Relevant for business transfer cases i.e. merger/amalgamation/de-merger
 - Business transfer approved by Court with prior effective date
 - Intervening period:
 - Period between the effective date (means appointed date as per Company law and Court Order date)
 - In such a case, there could be transactions of sale, manufacture, services, etc between the two companies in the intervening period

Appointed date (as per Company law)	01 April 2012
High Court order date	01 December 2012
Effective date as per High Court	01 July 2012

Business re-organization - Indirect Tax implications

Intervening period transactions

- Business transfer - Central Excise, Customs & Service Tax
 - No specific provision for taxability of transactions between companies in the intervening period
 - Practically, since tax registrations to new companies are granted only after receiving High Court order, typically, indirect taxes on transactions between companies in the intervening period are being paid
 - Even CENVAT credit balance is allowed to be transferred as per CENVAT Credit Rules, 2004 as appearing on the Court order date

Business re-organization - Indirect Tax implications

Intervening period transactions

- **Business transfer - VAT/CST**
 - State specific provisions to be referred
 - As per the MVAT provisions, VAT implications on transactions between companies in the intervening period would be as follows:
 - **Amalgamation** - sale and purchase of goods shall be considered in the purchase or sale turnover of respective companies and be liable to VAT
 - **Demerger** - it would be presumed that companies arising out of demerger have not purchased or sold any goods to each other during the period from the effective date and the court order date (i.e. from 1 July to 1 December 2012)
- Transactions stipulated: merger/amalgamation/de-merger
 - Situation of slump sale?
 - **Effective date as per Business Transfer Agreement (BTA)**

Business re-organization - Indirect Tax implications

Tax credits - Central Excise & Service Tax

- As per Rule 10 of the CENVAT Credit Rules, 2004, if a factory is transferred on account of sale, merger, amalgamation, lease, the unutilized balance of CENVAT credit can be transferred to the new entity provided liabilities of such factory is also transferred to the new Company
- The CENVAT credit in respect of inputs and capital goods would be allowed to be transferred only if the said inputs and capital goods are also transferred to the new entity
- For this purpose, the inputs and capital goods transferred to the New Co should be accounted for to the satisfaction of the jurisdictional AC or DC
- CENVAT credit cannot be transferred in case of itemized sale of assets

Business re-organization - Indirect Tax implications

Tax credits - VAT/CST

- As per Section 55(7) of the MVAT Act, where a dealer transfers or otherwise disposes of his business in whole or in part or effects any change in the ownership thereof, in consequence of which he is succeeded in the business or part thereof, by any other person
- In view of the above, transfer of input tax credit should be permitted in case of whole or part transfer of business or change in ownership
- Input tax credit cannot be transferred in case of itemized sale of assets

Business re-organization - Indirect Tax implications

IDT incentives

- Export incentive schemes under Foreign Trade Policy
 - Where the transferor company holds entitlements under export incentive schemes such as EPCG, Advance license, etc, transfer of such licenses to the transferee company would be subject to conditions applicable to the respective schemes
 - EPCG license and Advance authorization are subject to ‘actual user condition’
 - Specific permissions would need to be obtained from the DGFT for transfer of export incentive licenses and goods imported under the schemes
 - DEPB licenses are freely transferable without any restrictions

Business re-organization - Indirect Tax implications

IDT incentives

Sales tax incentive schemes

- Transfer of entitlements under the sales tax incentive schemes would be subject to the conditions and procedures as stated in the respective schemes and the MOU signed with the State Government are generally transferrable
- Incentive schemes can not be transferred in case of itemized sale of assets

Business re-organization - Indirect Tax services

Compliances and procedures

- **Registration**
 - Cancelling /amending registration of transferor
 - Obtaining new registration /amending registration of transferee
- **Intimation to/permission from appropriate authorities**
 - Tax assessing authorities
 - Appellate authorities
 - Authorities granting and assessing tax incentives
- **Necessary compliance for**
 - Transfer of tax credit balance
 - Issue and collection of statutory declaration and forms

Business re-organization - Indirect Tax implications

- Tax structuring consulting:

- Determine and shape the immediate and long-term tax impact of a client's acquisitions and dispositions

- Tax Due Diligence:

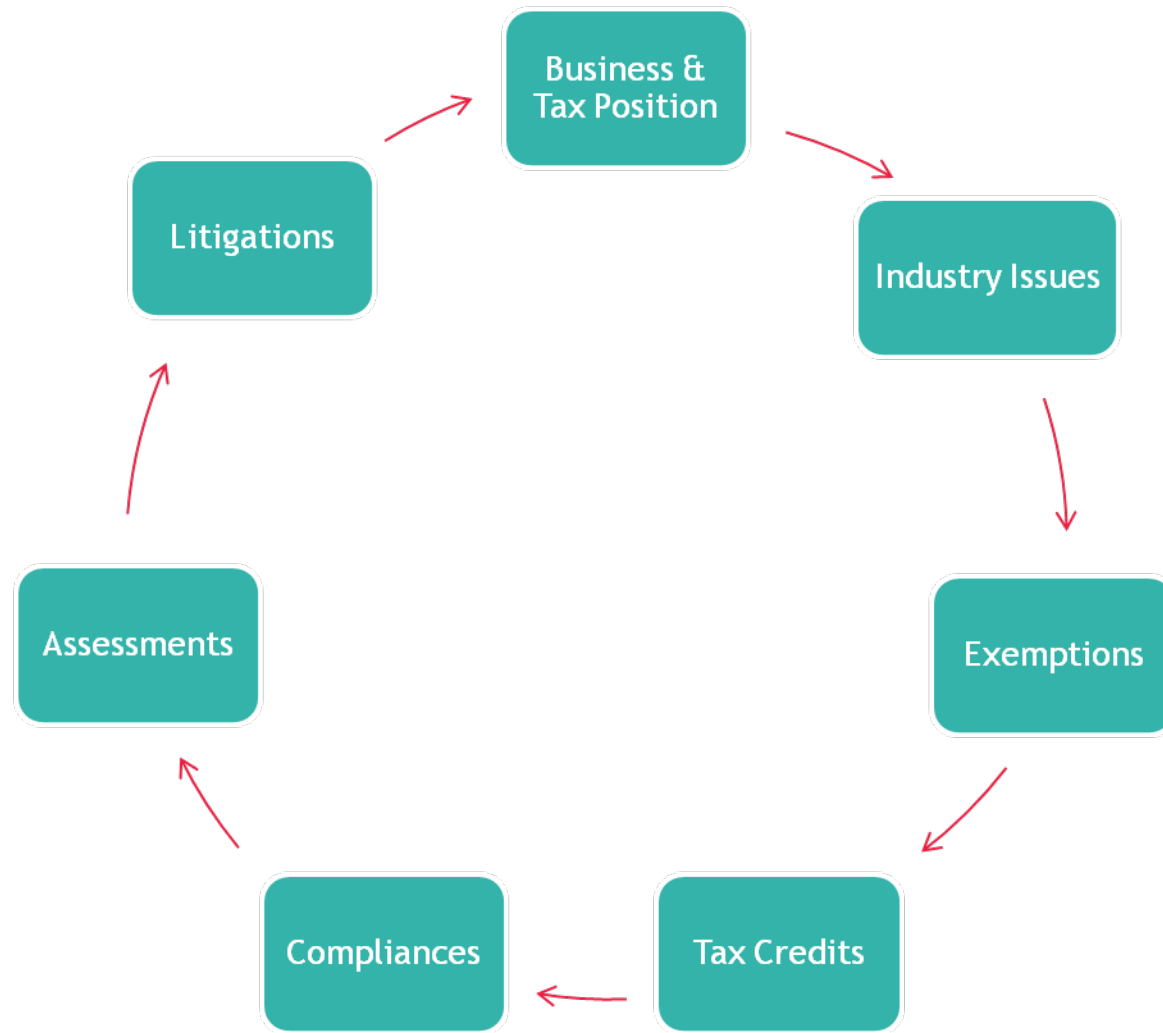
- Appraise clients of the potential risks and benefits associated with a specific transaction

- Post-Transaction Tax Integration Services:

- Determine the most tax efficient structure and way to combine and the target and acquirer following the transaction

Business re-organization - Indirect Tax implications

- Tax Due Diligence



Business re-organization - Indirect Tax implications

- Tax Due Diligence - key documents for review
 - Audited Financial statements for past 3-5 years
 - Trial balance thereafter upto the period of due diligence
 - Business & product/service profile
 - Tax audit report
 - VAT audit reports
 - Statement of Contingent liability
 - Trial Balance (grouped)
 - Returns & Payment Challan with workings & reconciliations
 - Tax exemption documents (PSI, SSI, Area based exemptions)
 - List of open assessments and litigations
 - EA-2000 / CERA or Business audit reports
 - Notices, letters of tax authority seeking details/ raising questions

