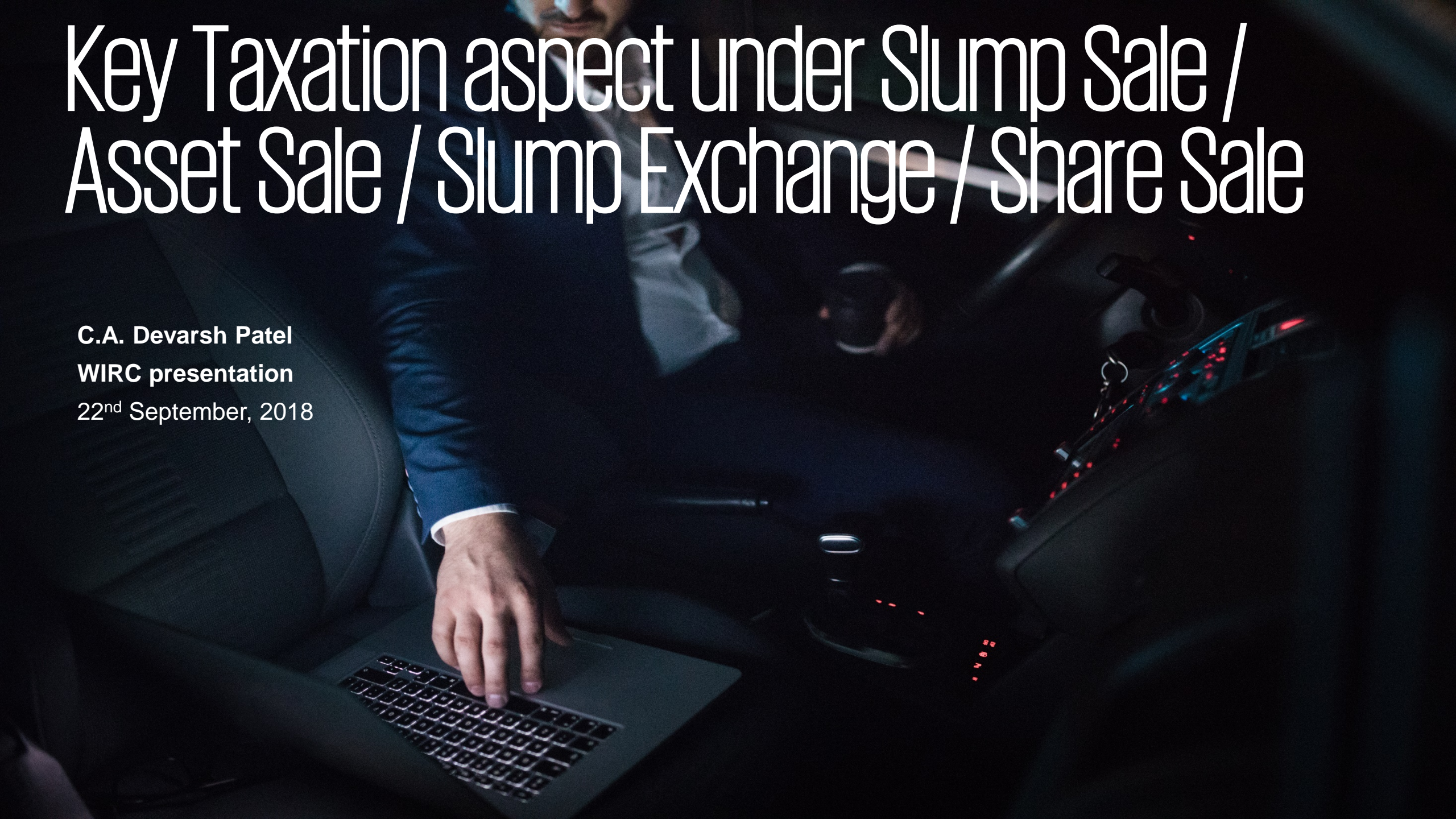


Key Taxation aspect under Slump Sale / Asset Sale / Slump Exchange / Share Sale

C.A. Devarsh Patel

WIRC presentation

22nd September, 2018



Topic Overview



Slump Sale

- ✓ Transfer of an undertaking on a going concern basis (“as is where is” basis) for a lump-sum consideration

Slides 3 - 18

Itemized Sale

- ✓ Individual sale of assets where consideration is identifiable against each asset

Slides 20 - 23

Share Sale

- ✓ Transfer of business via sale of shares of transferor undertaking

Slides 25 - 29

Slump Exchange

- ✓ Transfer of exchange through non-monetary consideration

Slides 31 - 35



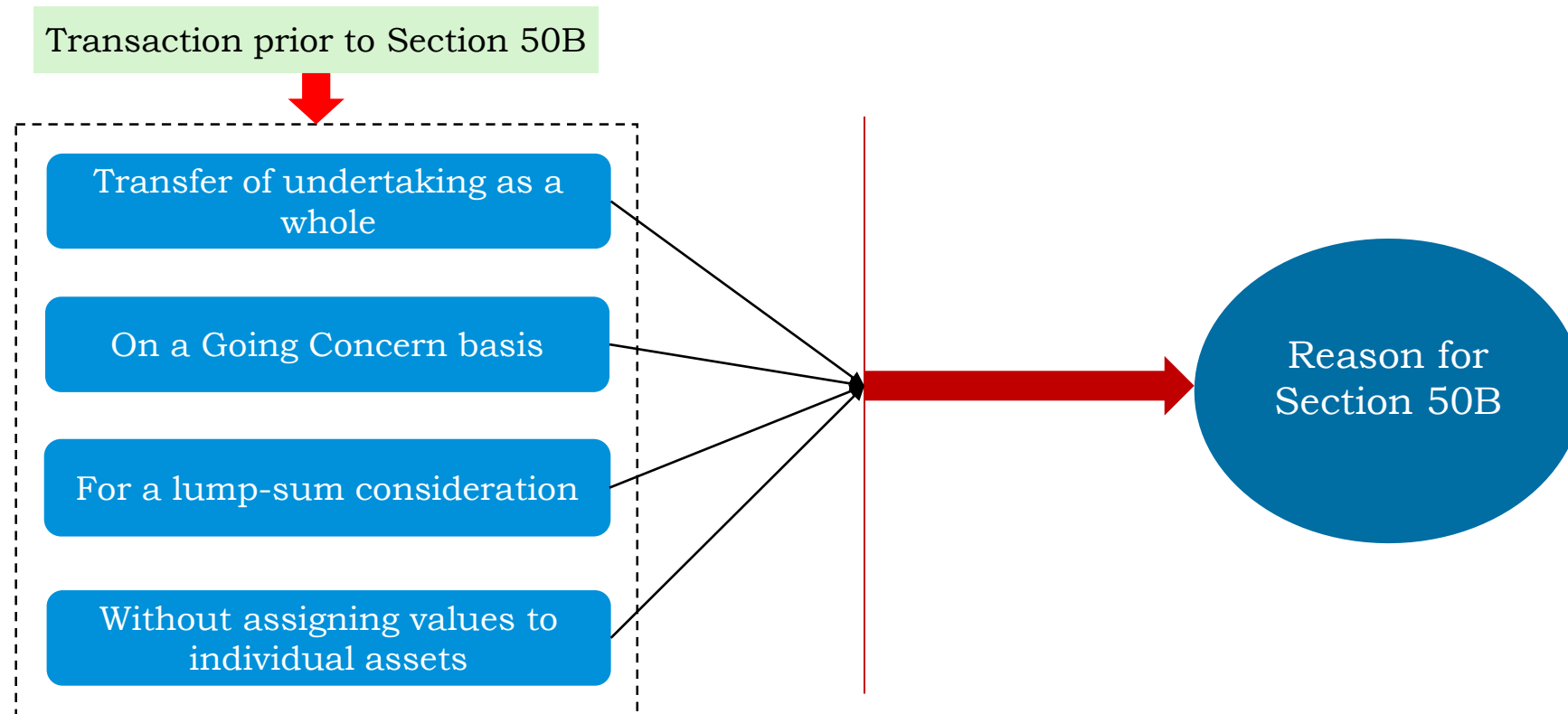
Slump Sale

WIRC Presentation – 22nd September, 2018

Why Section 2(42C) and Section 50B were introduced?



- **Section 2(42C)** : Definition of the term ‘Slump Sale’
- **Section 50B** : Special provision for computation of capital gains in case of slump sale



Slump Sale



- Transfer of undertaking as a going concern for slump consideration (either in cash or in the form of shares) not liable to capital gains:
 - Transaction chargeable to tax u/s 45 but computation to be in accordance with section 48 for determination of COA and COI
 - Since no value assigned to individual assets, the cost of undertaking and cost of improvement not ascertainable
 - As the computation mechanism fails, charging provision also fails and accordingly, not liable to capital gains
- The above was held by SC in the case of
 - *PNB Finance Limited [2008] 175 Taxman 242*
 - *Electric Control Gear Mfg Co [1997] 93 Taxman 384*
- However, contrary view was taken by SC in case of *Artex Mfg Co [1997] 93 Taxman 357* in which the transfer of undertaking was held as taxable u/s 41(2)

Section 50B introduced w.e.f. September AY 2000-01 as “Special provision for computation of capital gains in case of slump sale” - **CBDT Circular 779 dated 14 1999** (Applicable Prospectively)

Section 2(42C) - Definition



Definition

Per section 2(42C) of Income-tax Act ('ITA') - "Slump Sale" means :

- ✓ transfer of one or more **undertakings**
- ✓ sale for a **lump sum consideration**
- ✓ **without values being assigned to individual assets and liabilities**

"Undertaking" will have the meaning assigned to it in Explanation 1 to section 2(19AA)

"Undertaking" to include within its scope

- ✓ **any part of an undertaking,**
- ✓ a unit or division of an undertaking,
- ✓ **a business activity taken as a whole**

but **does not include individual assets or liabilities** or any combination thereof **not constituting a business activity.**

Explanation - Determination of value of an asset or liability for payment of stamp duty, registration fees etc. shall not be regarded as assignment of values to individual assets or liabilities

Whether following Assets/Liabilities constitute an undertaking?



Whether transfer of following combinations of assets and liabilities constitute an undertaking?

Asset exclusion
Transfer of assets without liabilities <i>Mahindra Sintered Products Ltd. v. DCIT, [95 ITD 380 (Mum.)</i> <i>Weikfield Products Co. (I) (P.) Ltd. v. DCIT, [71 TTJ 518 (Pune)]</i>
Transfer of assets and payment of liabilities
Business transferred without sundry debtors <i>Premier Automobiles vs ITO [2003] 129 Taxman 289 (Bom)</i>
Manufacturing and distribution undertaking transferred of without excess land, vehicle & debtors <i>DCIT vs Mahalasa Gases & Chemicals (84 TTJ 992) (Bang)</i>
Manufacturing division transferred –Technical know-how transferred in subsequent period; <i>Max India Ltd [112 TTJ 726]</i>
Transfer of BIFR unit – whether going concern or not? <i>KBD Sugars & Distilleries Ltd. v. ACIT (ITA Nos.1362&1363/ Bang/ 2011)</i>
Transfer of business without employees

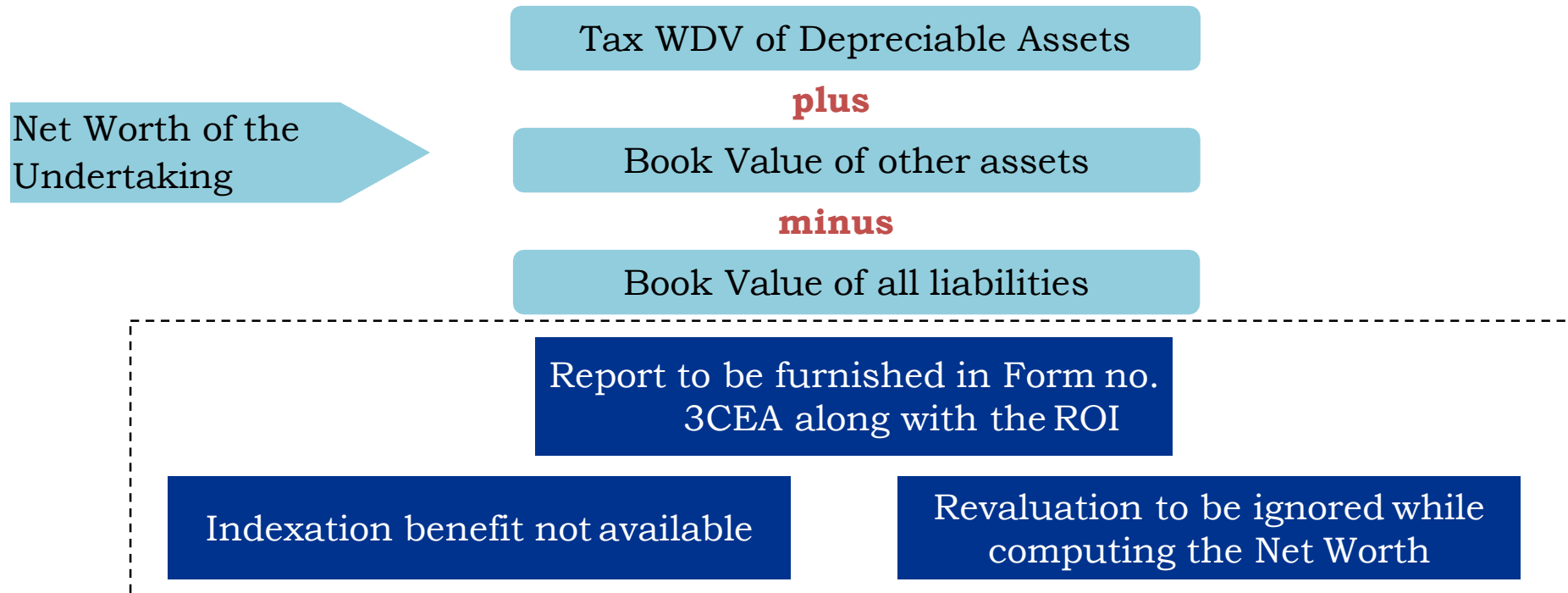
TEST : Business Undertaking should be able to run independently

Section 50B – Tax Implications – For the Seller



Computation of capital gains - Section 50B

- Consideration as reduced by Net Worth (deemed COA) of Undertaking
- Net worth = Aggregate value of total assets of the undertaking (less) Book value of liabilities of such undertaking
- Long Term Capital Gains, if Undertaking is held for more than 3 years





Case #1 – Determining WDV

Particulars	Total	Block of Assets		
		Asset 1	Asset 2	Asset 3
As on April 1, 2016 (Original Cost)	100	50	20	30
Sold during FY 16-17	(50)			(50)
WDV as on March 31, 2017	50			
Depreciation @ 10%	(5)			
WDV as on April 1, 2017	45			

FY 17-18,
sold in
slump sale

What will be the WDV of the asset transferred on slump sale:

1. 45 i.e. 50 less 5 (depreciation) OR
2. 46.5 i.e. 50 less 3.5 (proportionate depreciation)

Facts of the case:

- The block of assets comprises only of 3 assets
- During the FY 16-17, asset originally of INR 30 was sold for INR 50
- During FY 17-18, asset originally of INR 50 was sold as slump sale

Section 43(6)



Case #2 - Eligibility to claim Depreciation

Background

- Company A installed a solar power plant to venture into power generation business.
- In the first year of installation, company A claimed 100% depreciation on the cost of the power plant as per section 32(1)(ii) and 32(1)(iia) of the Income-tax Act, 1961.
- After 3 years, another Indian private company B purchases the power generation business by way of slump sale.
- Company B to pay cash consideration of 180 (i.e. value of power plant as per valuation report 200 less debt taken over 20)

Whether company B is eligible to claim depreciation on:

1. 200 i.e. value of power plant as per valuation report **OR**
2. 100 i.e. company A's book value of power plant **OR**
3. 0 i.e. company A's tax WDV of power plant?

Case Laws

- Shreyans Industries Ltd – Punjab & Haryana HC [149 taxman 373]
- South Asia Tyres Ltd – Pune ITAT [157 taxman 198]
- Lafarge India Ltd – Mumbai ITAT [9 taxmann.com 40]

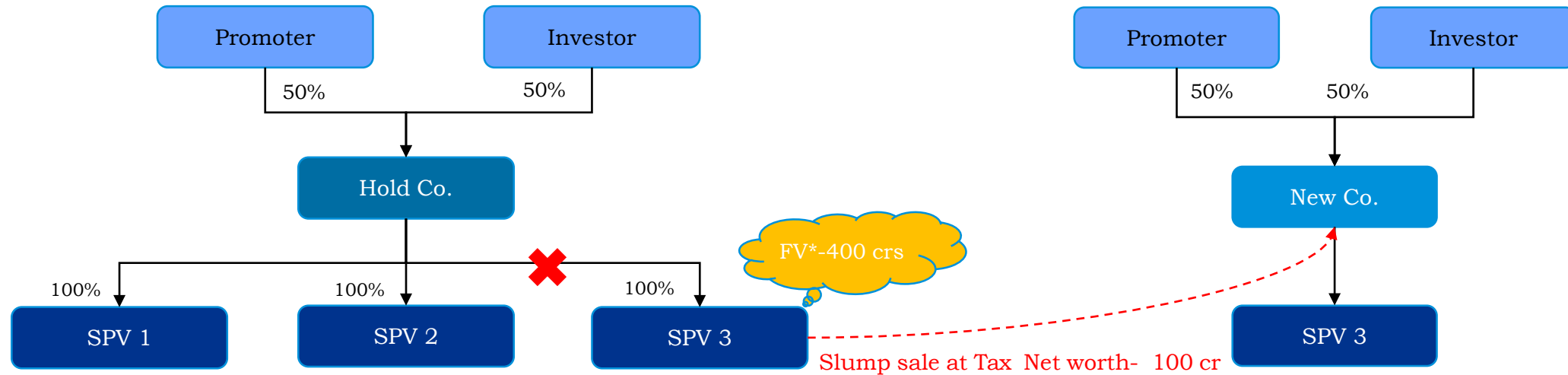
It was held in case of United Breweies Ltd that the scope and objective of the Expl.3 of Section 43(1) of the Act is to check the excess claim of depreciation by enhancing cost of assets acquired which were already in use by other person .

Balance Sheet – Company A

Liabilities	INR	Assets	INR
Equity	80	Power Plant (Tax WDV is Nil)	100
Debt	20		
Total	100	Total	100

Section 43(1) Exp. 3

Case #3 – Section 50B v Section 50CA



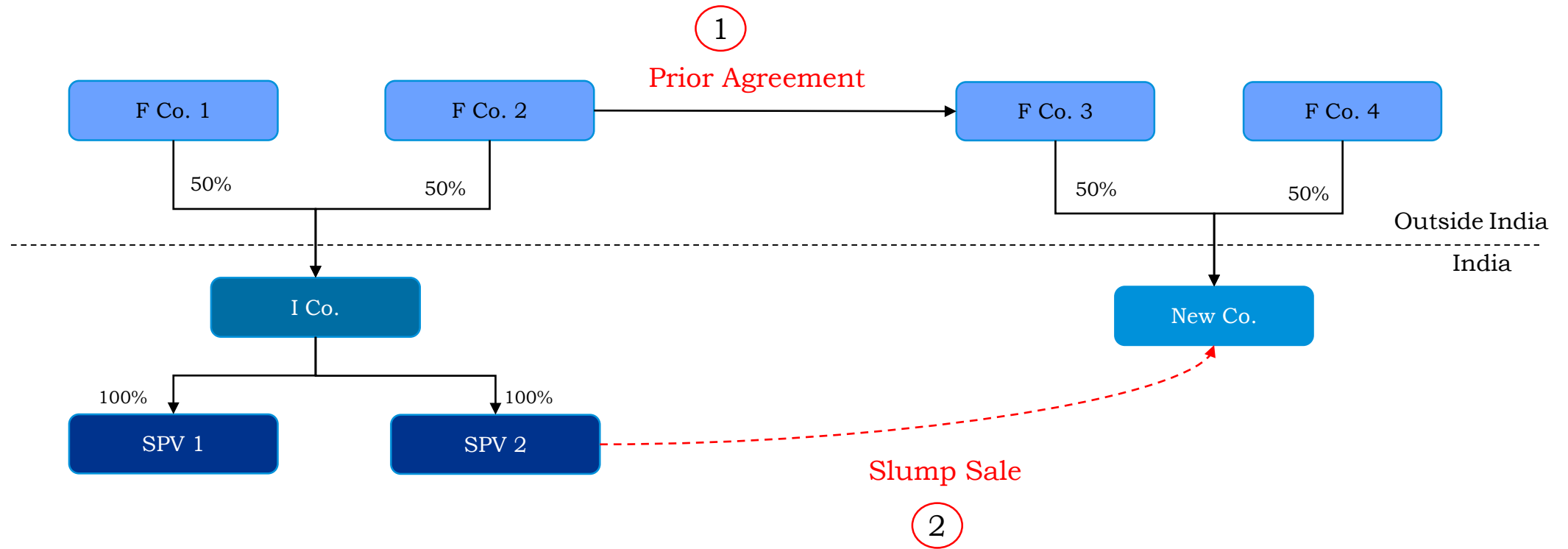
Facts of the case:

- Hold Co is engaged in business of developing real estate and each company represents a separate real estate project
- Promoters and Investors have incorporated a New co in same proportion as in Hold Co
- Hold Co to Slump sale its investment in SPV 3 at tax net worth amounting to INR 100 cr (value basis Section 50Ca read with rule 11UA~ INR 400cr)

Whether 50CA would be invoked on transfer of Investment in SPV 3 ?

* Value calculated basis Section 50Ca read with rule 11UA

Case #4 – Slump sale amongst foreign owned entities



Whether Transfer Pricing Provisions will apply?

Case #5 – Whether profits under Section 50B can be used to set-off B/F business losses?



Particulars	Scenario A	Scenario B
Short term Capital gains computed under Section 50B	150	150
Brought forward business Loss	50	50
Less: set off under Section 72(1)	(50)	-
Taxable STCG under Section 50B	100	150



Which of the scenario represents the correct computation of income?

Digital Electronics Ltd v. ACIT [(2011)] ITA No. 1658/ Mum/ 2009]	Mumbai ITAT held that profit realized on sale of business asset although assessable under the head 'Short-term capital gain' is business income and accordingly brought-forward business losses should be set-off as per Section 72 of the ITA
Nandi Steels Ltd. v. ACIT [(2011) ITA No. 546/Bangalore/2008]	The Special bench held that Capital gains arising on sale of capital assets used for the purpose of business could not be referred to as business income and it could not be set-off against brought forward business losses of earlier years.
M/s Mipco Seamless Rings Vs. ACIT [(2012) ITA No 2680/Mum/2010]	Referred Digital Electronics (supra) and Nandi Steels (supra). However, judgment in case of Nandi Steels was delivered by the larger bench, hence, Nandi Steels was followed
Sac Steel Rolling Mills Pvt v. JCIT [(2016) ITA No 652/PN/2013]	Pune ITAT referring to Nandi Steels (supra) held that Capital gains arising on sale of capital assets used for the purpose of business could not be referred to as business income and it could not be set-off against brought forward business losses of earlier years

Case #6 - Transfer of undertaking with “NEGATIVE” networth



Particulars	Amount Rs
Sales consideration	100
Less:	
Cost of acquisition (networth)	
Aggregate value of total assets	300
less total value of liabilities	(500)
	(200)
Capital gains - negative networth ignored)	100

Particulars	Amount Rs
Sales consideration	100
Less:	
Cost of acquisition (networth)	
Aggregate value of total assets	300
less total value of liabilities	(500)
	(200)
Capital gains - negative networth (100-[-200])	300



Which of the scenario represents correct computation of capital gains

SRM Energy Limited v. DCIT (2015)
ITA No 495/Mum/2012

Mumbai ITAT following the decision of Summit Securities (supra) held that Negative Net worth will not be assumed as “Nil” ,i.e. it will added to Full value of consideration for computation of Capital Gain Tax.

DCIT v. Summit Securities Ltd (ITA
No. 4977/ Mum/ 2009)

Special Bench of Mumbai ITAT held that negative net worth of the undertaking should not be ignored for working out capital gains in case of a slump sale u/s 50B of the ITA

Zuari Industries Ltd. v. ACIT [(2007)
105 ITD 569 Mum]

Mumbai ITAT had held that negative net worth of the undertaking transferred would be would be taken as "Nil" which shall be deemed to be the cost of acquisition for the purpose of computing capital gain u/s 48 of the ITA

Case #7: Depreciation on Slump Sale (1/2)



Which is the correct way to compute depreciation in case of slump sale?

Eg 1 : Date of slump sale – January 1, 2015

Seller

Particulars	Amount (in INR Crs)
WDV of block of assets	1000
WDV of block of assets transferred pursuant to slump sale	100
Depreciation on assets transferred (proportionate) $(100 \times 9 / 12 \times 25\%)$	(18.75)
Depreciation on remaining block @ 25%	225

Buyer

Particulars	Amount (in INR Crs)
Consideration paid	200
Less: proportionate depreciation $(200 \times 3 / 12 \times 25\%)$	(12.5)
WDV available	187.5

Eg 2 Seller

Particulars	Amount (in INR Crs)
WDV of block of assets	1000
WDV of block of assets transferred pursuant to slump sale	100
Depreciation on assets transferred (proportionate)	-
Depreciation on remaining block @ 25%	225

Buyer

Particulars	Amount (in INR Crs)
Consideration paid	200
Less: proportionate depreciation $(200 \times 25\% \times 1/2)$	(25)
WDV available	175

Case #7: Depreciation on Slump Sale (2/2)



Eg
3

Seller

Particulars	Amount (in INR Crs)
WDV of block of assets	1000
WDV of block of assets transferred pursuant to slump sale	100
Depreciation on assets transferred (proportionate) (100*9/12*25%)	(18.75)
Depreciation on remaining block @ 25%	225

Buyer

Particulars	Amount (in INR Crs) – Yr 1
Consideration paid	100
Less: proportionate depreciation (100*3/12*25%)	(6.25)
WDV available	93.75

As per proviso 5 to Section 32, aggregate deduction in respect of depreciation of tangible and intangible assets in case of succession as per S. 170 shall not exceed in any year previous year the deduction that would have been available to the predecessor assuming no succession took place.

As per 49(6)(C), WDV in the case of slump sale would be as under:

Actual cost of the asset as reduced by the depreciation from the date of purchase till the previous year relevant to the assessment year in which it is transferred as if it is only asset in the block of asset



Case #8: Section 50B vs Section 47(iv)/47(v)

✓ A Co does a slump sale of business Undertaking to B Co under Section 50B



✓ Whether 47(iv) is mandatory?

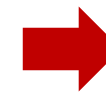
✓ Whether transaction would not be treated as transfer under Section 47(iv) and not chargeable to capital gains tax?

- Section 50B a charging provision or computation mechanism section?
- PNB finance Ltd (SC) (2008) and Marudhar Hotels (Jodhpur Tribunal) (2013) **vs.** AAR ruling in RST (2012), Industrial Machinery Associates (Abad ITAT) (2012)



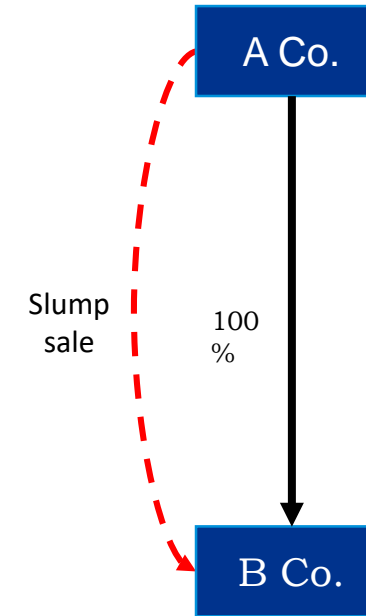
✓ If yes, what would be the cost of acquisition of the undertaking in the hands of B Co

- at fair value or at book value
- Explanation 6 to Section 43(1) and Explanation 2 to 43(6)(c)
- Essar Oil limited MUM Tribunal (2007)



Idea to circumvent Section 47(iv)?

Section 43(1) Exp. 6





GST implications

✓ Rule 41 of Central Goods and Services Tax (CGST), 2017

Slump Sale entails a “sale of business on a going concern basis”. Accordingly, there shall be no GST implications on Slump Sale so long as Business undertaking is transferred on a going concern basis.

✓ Sub section (3) of Section 18 of the The Central Goods and Services Tax Act, 2017

On transfer of the business with specific provisions for the transfer of liabilities, the registered person shall be allowed to transfer the input tax credit which remains unutilised in his electronic credit ledger to such transferred business



Itemized Sale

WIRC Presentation – 22nd September, 2018

Itemized Sale - Meaning



Meaning

- ✓ Not defined under ITA
- ✓ Involves individual sale of assets
- ✓ Consideration is identifiable against each asset
- ✓ Buyer discharges consideration to the seller for the asset acquired
- ✓ Not necessary what is transferred constitutes a business undertaking

Discretion available to acquirer to take over only those assets which shall result into commercial advantage to the acquirer and will not be under obligation to acquire any other assets / liabilities

Also, elimination of succession related liabilities

Itemized Sale – Tax Implications



Nature of asset	Nature of income
Depreciable Assets	<ul style="list-style-type: none">- Provisions of section 50 applicable- Short term capital gains (if the consideration > WDV of the relevant block of asset)
Non – Depreciable Assets	<ul style="list-style-type: none">- Short term capital gains / Long term capital gains (Depending on the period of holding)
Current Assets	<ul style="list-style-type: none">- Business profits

Case Study – Itemized Sale v/s Slump Sale



Facts

- Company A has 3 undertakings - Block of assets of INR 1000 crs
- It proposes to transfer an Undertaking 1 having a WDV of INR 200 crs for a consideration of INR 500 crs
- Whether Itemized sale or slump sale is preferable

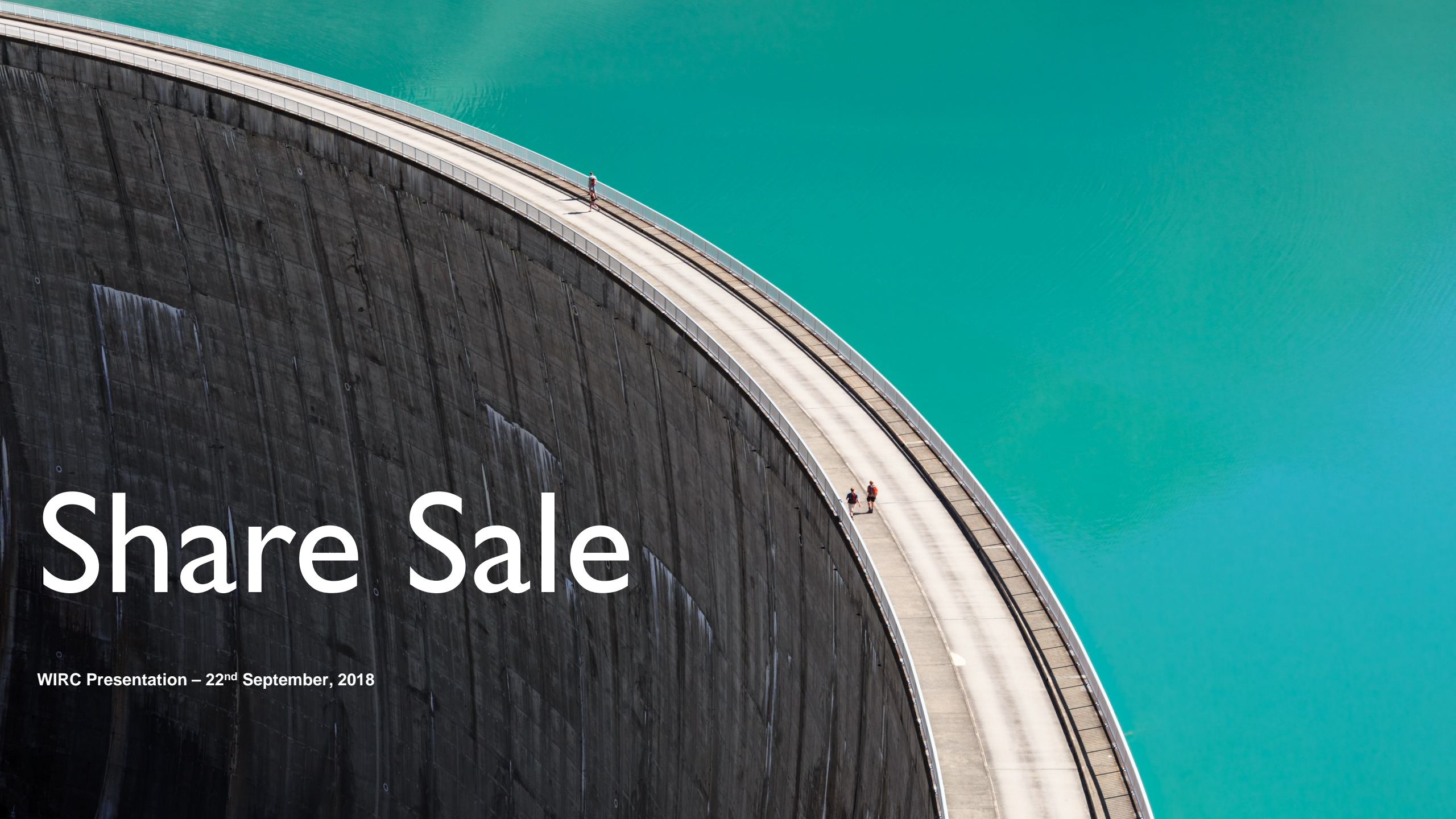
Particulars	Amount (in Rs)	Particulars	Amount (in Rs)
Block of assets	1000	Consideration received	500
Less: Consideration received	500	Less: Net worth of the undertaking 1 (WDV of the assets of undertaking 1)	200
Less: Actual cost of assets acquired during previous year	-	Long term capital gain (Assumed held for > 3 year)	300
Written down value	500	Taxable LTCG @ 20%	60



Round Up – Itemized Sale v/s Slump Sale



Particulars	Itemized Sale	Slump Sale
Criteria of 'undertaking'	Not required to be complied with	Required to be complied with
Nature of gains/loss	<ul style="list-style-type: none"> For depreciable assets – Short term For non-depreciable assets – Depends on the period of holding of assets 	<ul style="list-style-type: none"> Depends on the period of holding of the Undertaking Holding period of individual assets not relevant
Indexation benefit	Available (in case of long term assets)	Not available
Criteria for taking over 'Liabilities'	Flexibility of not acquiring the liabilities	No flexibility
Provisions of section 50C	Applicable	Not Applicable
Tax incentives	Not available	Available
Carry forward and set-off of losses	No	No



Share Sale

WIRC Presentation – 22nd September, 2018

Share Sale – Implications in the hands of the Seller



Capital gains tax / MAT on seller (including consideration received in the form of non compete fee) – Possible to mitigate / reduce by appropriate structuring depending upon facts of transaction (e.g. STCG v/s LTCG). Sale of shares to be in compliance with section 50CA and 56(2)(x) to avoid tax exposure (Refer subsequent slide)

Tax losses of transferor entity may lapse due to change in shareholding – Possible to protect through appropriate structuring basis relevant facts

Implication under the tax treaty need to be considered and planned appropriately to reduce the overall tax impact

Impact under indirect transfer provisions need to be considered for change in shareholding / control of Indian company pursuant to global acquisition

The tax benefit arising to the seller needs to be substantiated with commercial rationale to avoid any adverse implication under GAAR

Share Sale – Implications in the Hands of the Buyer



Past history of company, whose shares are being acquired, is to be inherited to transferee entity

Possible to mitigate the stamp duty implications on transfer of shares through dematerialization of shares

Withholding tax compliance by the buyer while making payment to non-resident seller

These risk are to be identified during due diligence process and mitigated through adjustment in valuation and / or appropriate indemnity and/or obtaining tax clearance certificate u/s 281 of IT Act

No GST implication on transfer of shares

Tax deductibility of interest on account of thin capitalization rules in India

Withholding tax compliance by the buyer while making payment to non-resident seller

Case Study – Transfer of Shares (1/2)



56 (2)(x) – in the hands of Recipient	50CA – in the hands of Seller
In a case where any person receives shares from another person, the difference between the aggregate fair market value of the shares received and the consideration paid, shall be chargeable to tax as income from other sources u/s 56(2)(x) in the hands of recipient, if it exceeds INR 50,000.	In a case where consideration received on transfer of unquoted shares, is less than the fair market value of shares, then for the purpose of computing gains, the full value of consideration

Case Study

Transfer of shares of XYZ Pvt. Ltd. by Mr. X to Mr. Y for INR 40,000 (FMV of shares is INR 100,000).
 Cost of Acquisition is INR 10,000. Assumed Indexed Cost is INR 27,000
 Period of Holding – greater than 24 months (Long term)

Particulars	Amount
Full Value of Consideration	100,000 (Section 50CA)
Less : Indexed Cost of Acquisition	(27,000)
Long Term Capital Gains taxable @ 23.296%	73,000

Also the difference between FMV and the consideration paid i.e. INR 60,000 shall be chargeable to tax as Income From Other sources in the hands of Mr. Y.

Case Study – Transfer of Shares (2/2)



56 (2)(viib) – in the hands of Issuer

Where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be chargeable to income-tax under the head "Income from other sources" in the hands of the Company

Case Study

Issue of shares of XYZ Pvt. Ltd. to Mr. Y for INR 400,000 (FMV of shares is INR 200,000)

Face Value of Shares INR 100,000

Particulars	Amount
Full Value of Consideration	400,000 (Section 50CA)
Less : FMV	(200,000)
Income from other sources	2,00,000

Case Study – Indirect Transfer



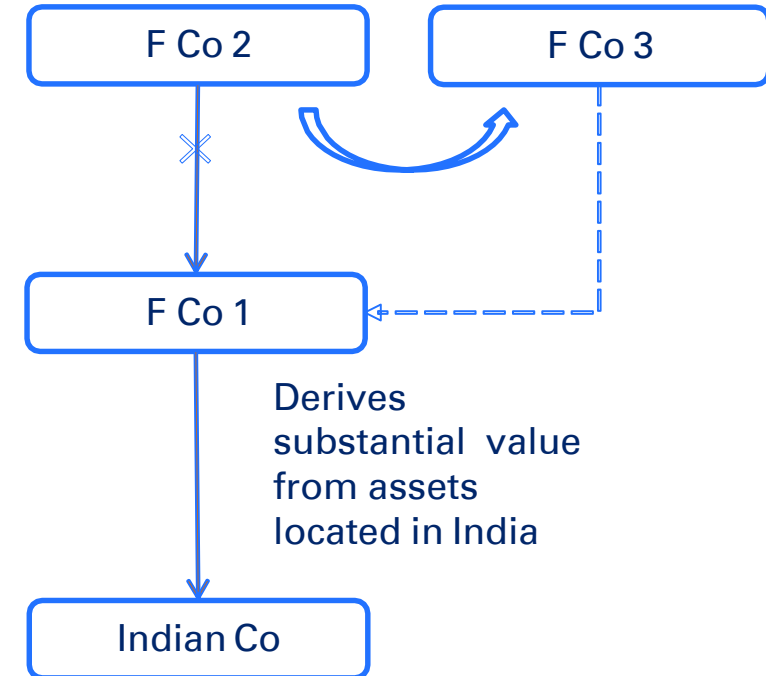
Background

Consider the following scenario:

- F Co. 1 holds 100% in Indian Co
- F Co. 2 holds 100% in F Co 1
- F Co 2 transfers its holding in F Co 1 to F Co 3

Provision

Section 9(1)(i) of the Income-tax Act, 1961 (Act) provides that income accruing or arising, whether directly or indirectly, inter-alia, through the transfer of a capital asset situated in India, shall be deemed to accrue or arise in India.





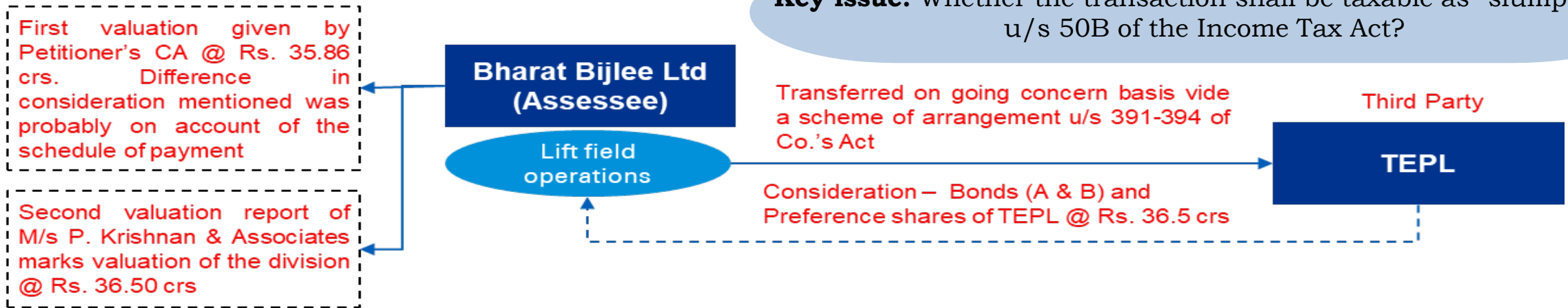
Slump Exchange

WIRC Presentation – 22nd September, 2018

Slump Exchange – Bharat Bijlee Ltd (Bom –HC) (1/2)



Key issue: Whether the transaction shall be taxable as “slump sale” u/s 50B of the Income Tax Act?

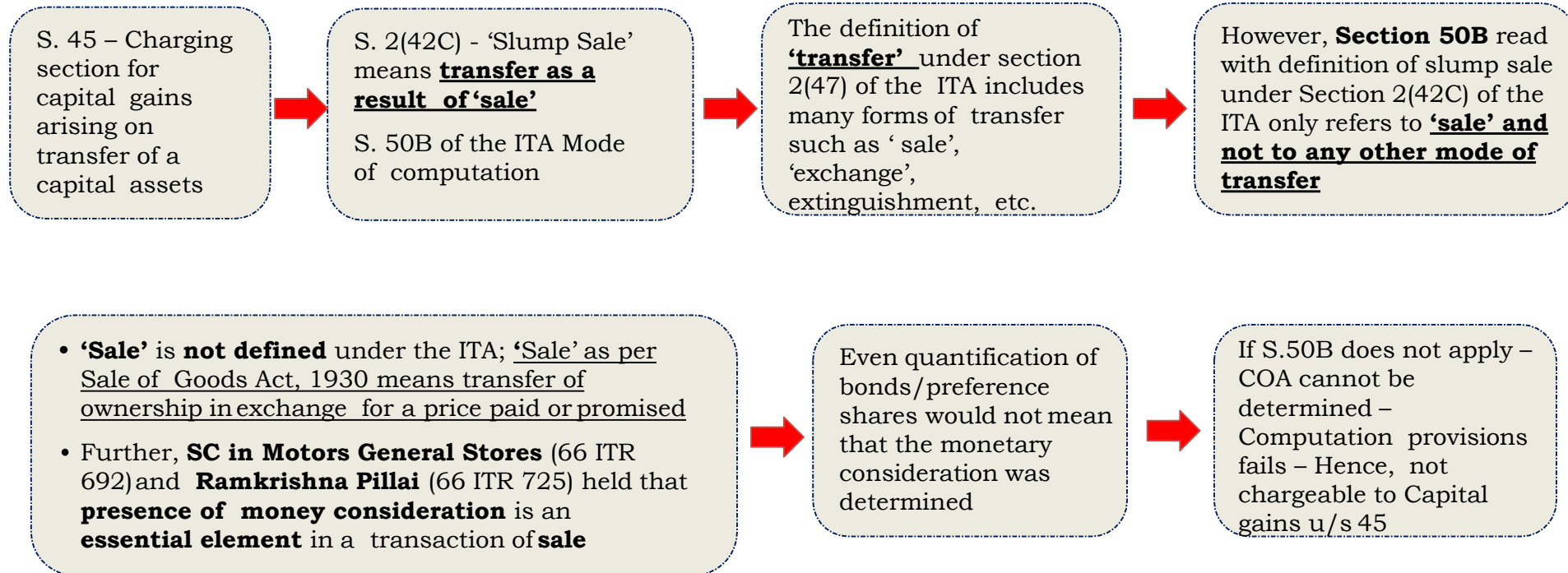


- ✓ Assessee contended that transfer is by way of exchange and hence out of purview of Section 50B and hence not chargeable to tax under Section 45 of the ITA
- ✓ **Revenue contended that transfer amounted to “sale” and not ‘exchange**
- ✓ ITAT had ruled in favour of assessee and held that transfer of the undertaking was neither a slump sale under S. 50B nor was it liable to capital gains tax under the general provisions
- ✓ Bombay HC also ruled in the favour of assessee and also distinguished a negative ruling by Mumbai ITAT on slump exchange in case of SREI Infrastructure [2012] 207 taxman 74/20

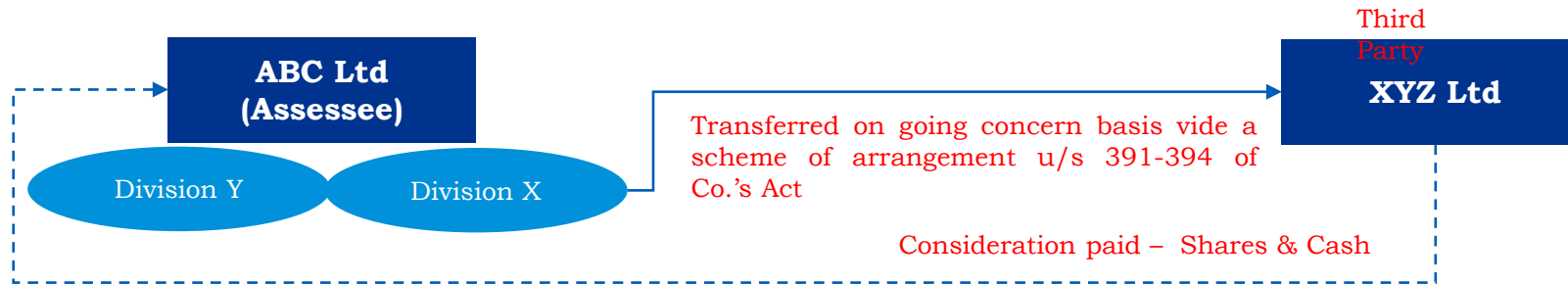
Slump Exchange – Bharat Bijlee Ltd (Bom –HC) (2/2)



Why not taxable



Favourable Judgment in case of Zinger investments Ltd



Mumbai ITAT in SREI Infrastructure Finance Limited

- **Section 50B was inserted to supersede decisions which held that a slump sale was not taxable for want of cost of acquisition**
- The word 'slump sale' has been defined in Section 2(42C) to mean transfer of one or more undertakings as a result of sale for a lumpsum consideration without values being assigned to individual assets and liabilities
- The term 'transfer' is with reference to the transaction in the nature of 'slump sale' – **accordingly, any type of transfer in the nature of slump sale is covered by the definition of Section 2(42C)**
- **Use of the word sale in the term slump sale is not intended to narrow down the concept of 'transfer' as defined in Section 2(47)**
- **Bharat Bijilee not referred in SREI Infrastructure Limited**

Slump Exchange – Implications in the hands of the Seller



What shall be the Cost of Acquisition of the instrument issued as consideration by the transferee to the transferor?

- ✓ Term 'Cost of acquisition' not defined under the ITA
- ✓ Determination of cost of acquisition of a capital asset under various situations defined in section 49, 50B, 55, etc
- ✓ Actual cost as per Section 43(1) of the ITA
 - However, no provision for determination of cost of acquisition of a capital asset acquired in exchange

At what value should the instrument allotted on the said exchange of Undertaking be recorded in the Books of the Transferor?

Whether Section 50D would apply in absence of determination of consideration?

Slump Exchange – Implications in the hands of the Buyer



How would the 'block of assets' of the transferor company be reduced in respect of depreciable assets transferred?

- ✓ As per S. 43(6)(c)(i)(B), moneys receivable to be deducted from the relevant block. However, no money rec'd, hence S. 43(6)(C)(i)(B) not applicable
- ✓ S. 43(6)(c)(i)(C) described mode of computation for slump sale – However, should also not be applicable in respect of transfer of undertaking by any mode other than slump sale.

Thank You

This views expressed in this presentation are personal views of the author. This presentation has been prepared for general guidance on matters of interest only and does not constitute professional advice. You should not act upon the information contained in this presentation without obtaining specific professional advice. The presentation should not be reproduced, in part or in whole, in any manner of form, without the author's permission
