

# Tax and Regulatory - Merger, Demerger & Restructuring

Hiren Bhatt

---

21 July 2018



# Glossary



<b>Abbreviation</b>	<b>Expansion</b>
---------------------	------------------

Bn	Billion
----	---------

CA 2013	Companies Act, 2013
---------	---------------------

CCI	Competition Commission of India
-----	---------------------------------

DDT	Dividend Distribution Tax
-----	---------------------------

FDI	Foreign Direct Investments
-----	----------------------------

GST	Goods & Service Tax
-----	---------------------

Hold Co	Holding Company
---------	-----------------

IPO	Initial Public Offer
-----	----------------------

I-GAAP	Indian General Accepted Accounting Principles
--------	---

Ind AS	Indian Accounting Standards
--------	-----------------------------

IT Act	Income-Tax Act, 1961
--------	----------------------

ITAT	Income Tax Appellant Tribunal
------	-------------------------------

INR	Indian Rupees
-----	---------------

# Glossary



<b>Abbreviation</b>	<b>Expansion</b>
---------------------	------------------

LRS	Liberalized Remittance Scheme
-----	-------------------------------

LODR	SEBI(Listing Obligation and Disclosure Requirements) Regulations
------	--

M&A	Mergers & Acquisitions
-----	------------------------

NCLT	National Company Law Tribunal
------	-------------------------------

OL	Official Liquidator
----	---------------------

POEM	Place Of Effective Business
------	-----------------------------

RD	Regional Directors
----	--------------------

ROC	Registrar of Companies
-----	------------------------

RBI	Reserve Bank of India
-----	-----------------------

Sub Co	Subsidiary Company
--------	--------------------

SE	Stock Exchange
----	----------------

USD	US Dollars
-----	------------

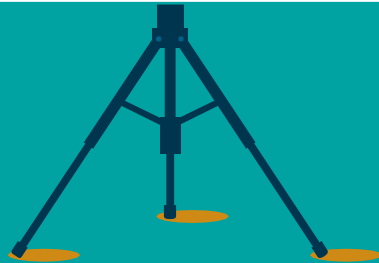
# Presentation Contents

**1 Background**

**2 Merger**

**3 Demerger**

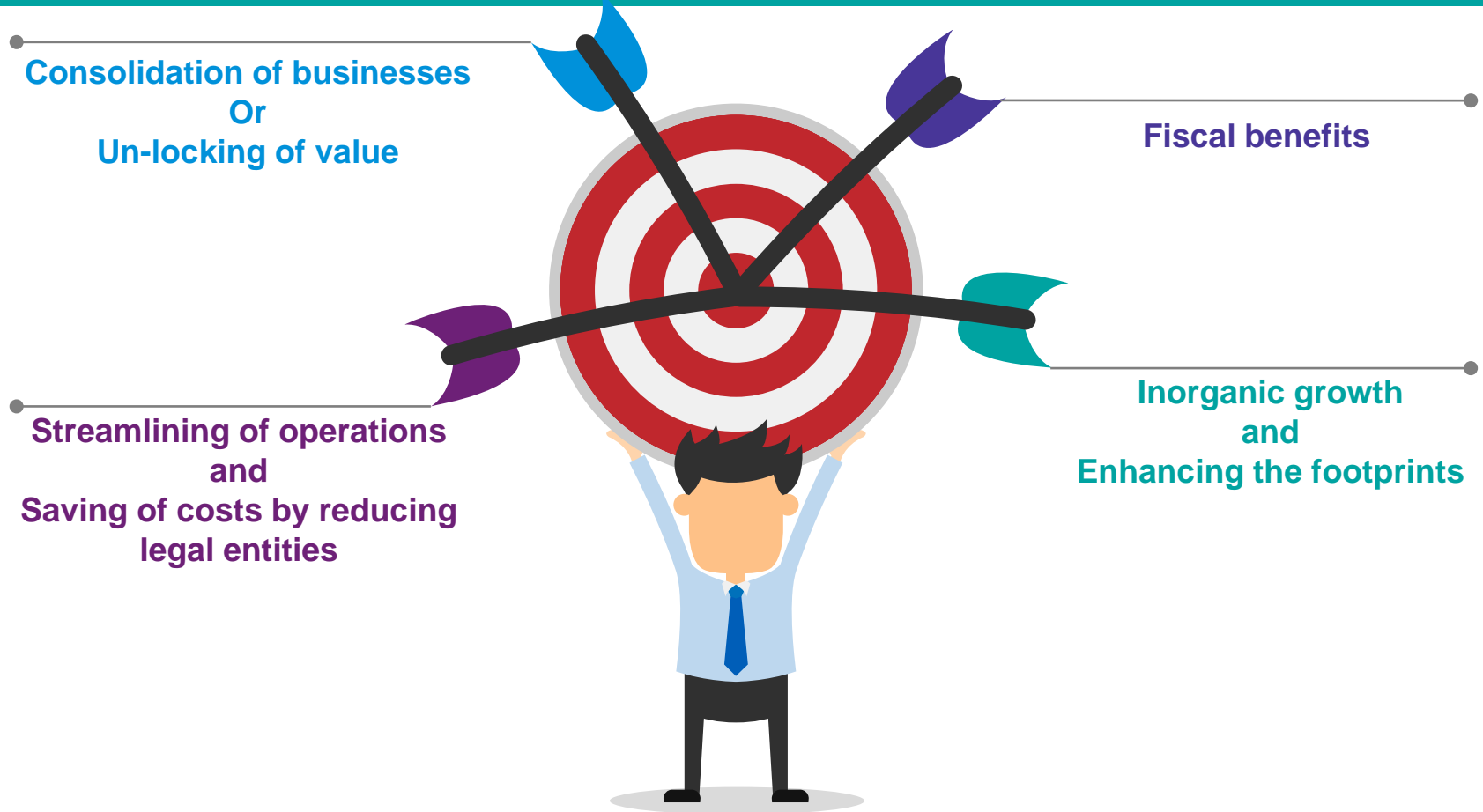
**4 Restructuring**



# Background



# M&A / Structuring Drivers



**While the above drivers are illustrative, corporate houses undertake M&A / Structuring for various reasons**

# Recent M&A transaction in India



**Vodafone India –  
Idea Cellular**

Acquisition through  
merger

**IDFC-Capital  
First**

Acquisition through  
merger

**Astral Pipes -  
Rex**

Acquisition through  
merger

**Growth and Enhancing the Footprints seems  
to be the key driver**

**HCL Tech –  
Geometric  
Solutions**

Acquisition through  
demerger

**Tele-Performance –  
Intelenet**

Acquisition-Share  
Purchase

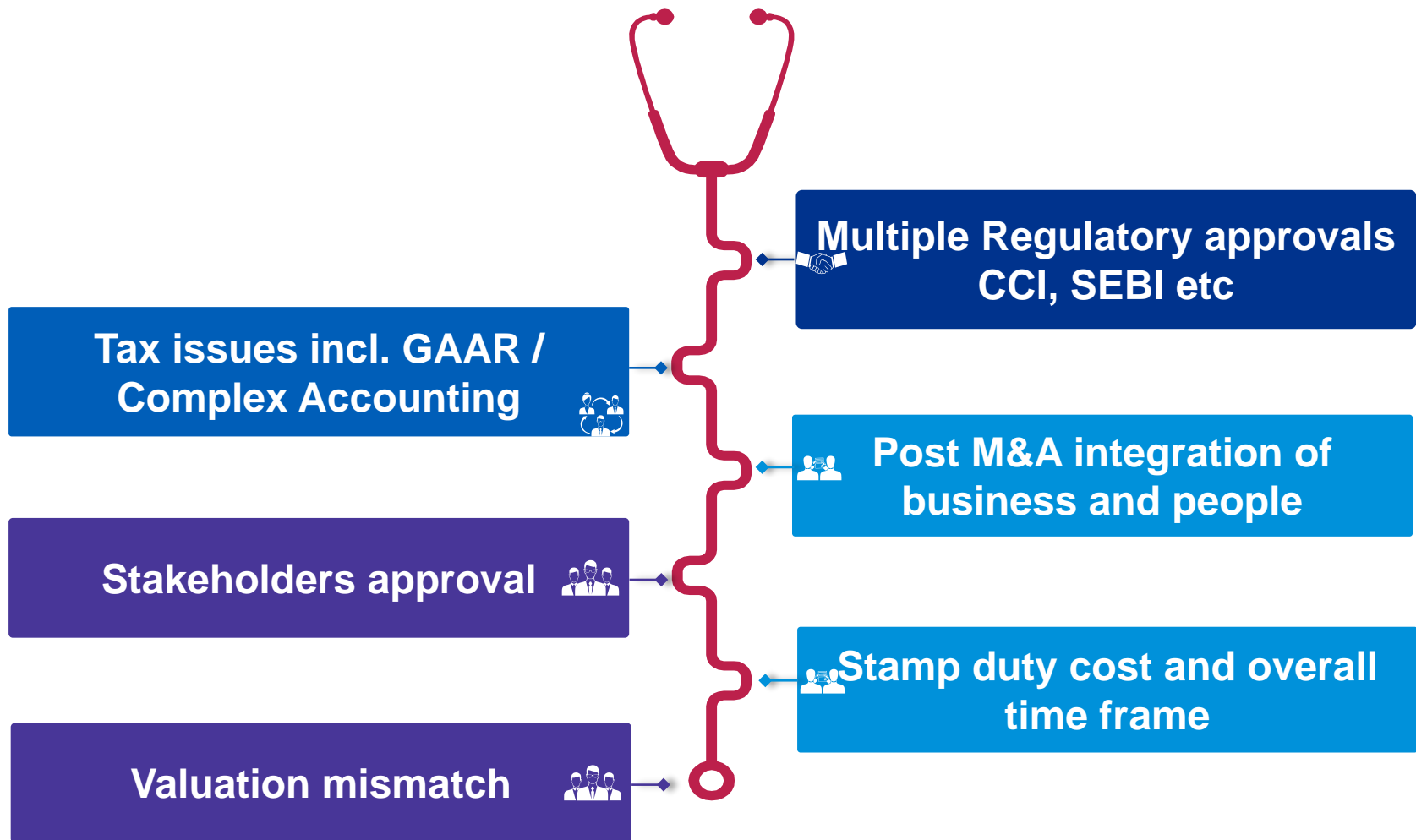
**Walmart-Flipkart**

Acquisition-Share  
Purchase

**Bharti Airtel Ltd  
– Telesonic  
Networks Ltd**

Acquisition through  
slump sale

# Key challenges in M&A / Restructuring





# Tax and Regulatory Scanner

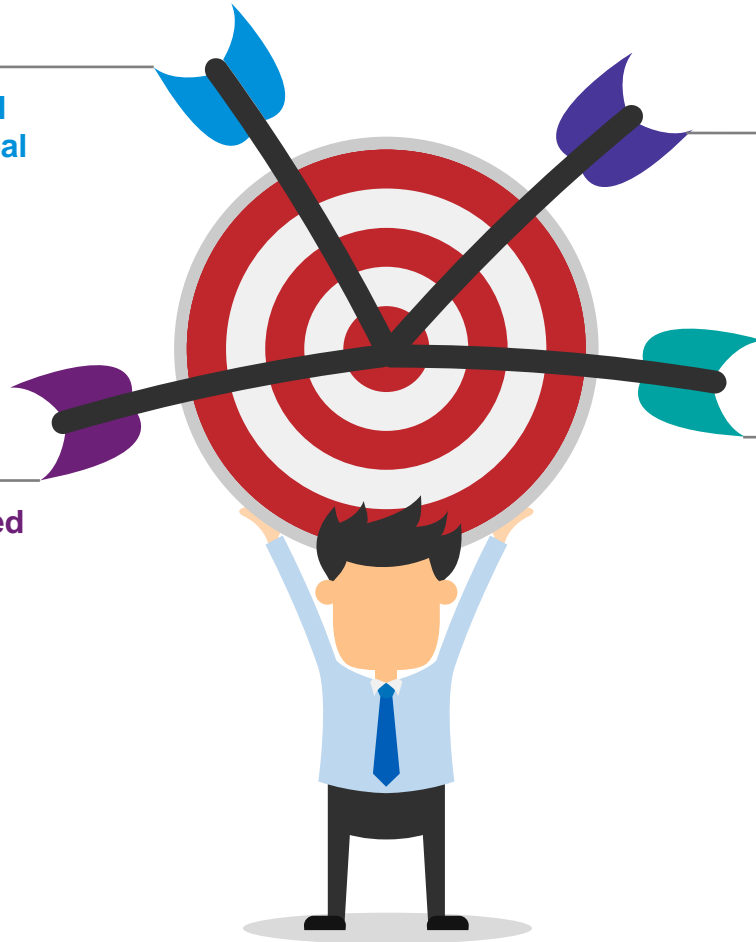


Withholding tax, CCI and FDI  
issue on Walmart Flipkart deal

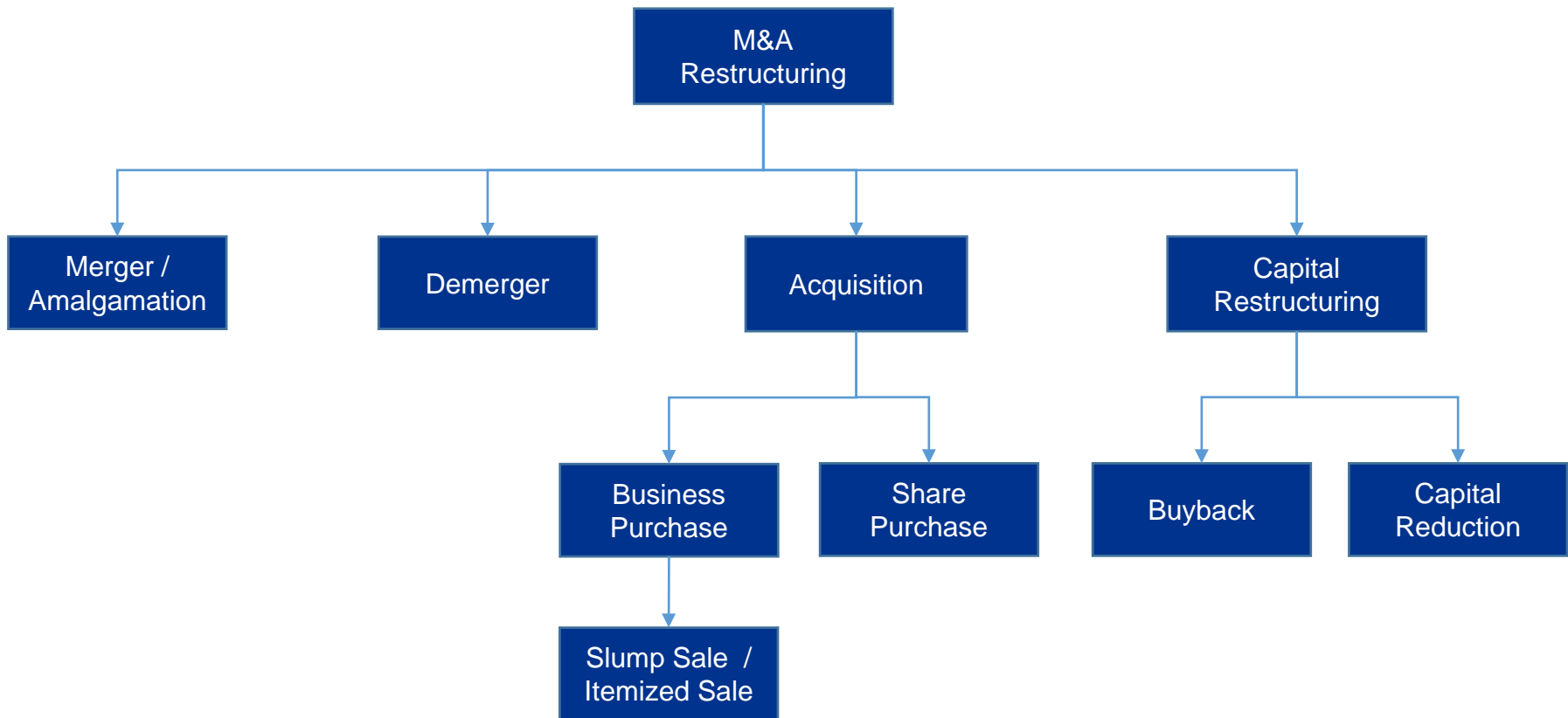
Buyback by Cognizant

HDFC life – MAX deal flopped  
– IRDA did not approve

R com Aircel merger called off  
due to legal and regulatory  
uncertainty



# Modes of M&A and Restructuring



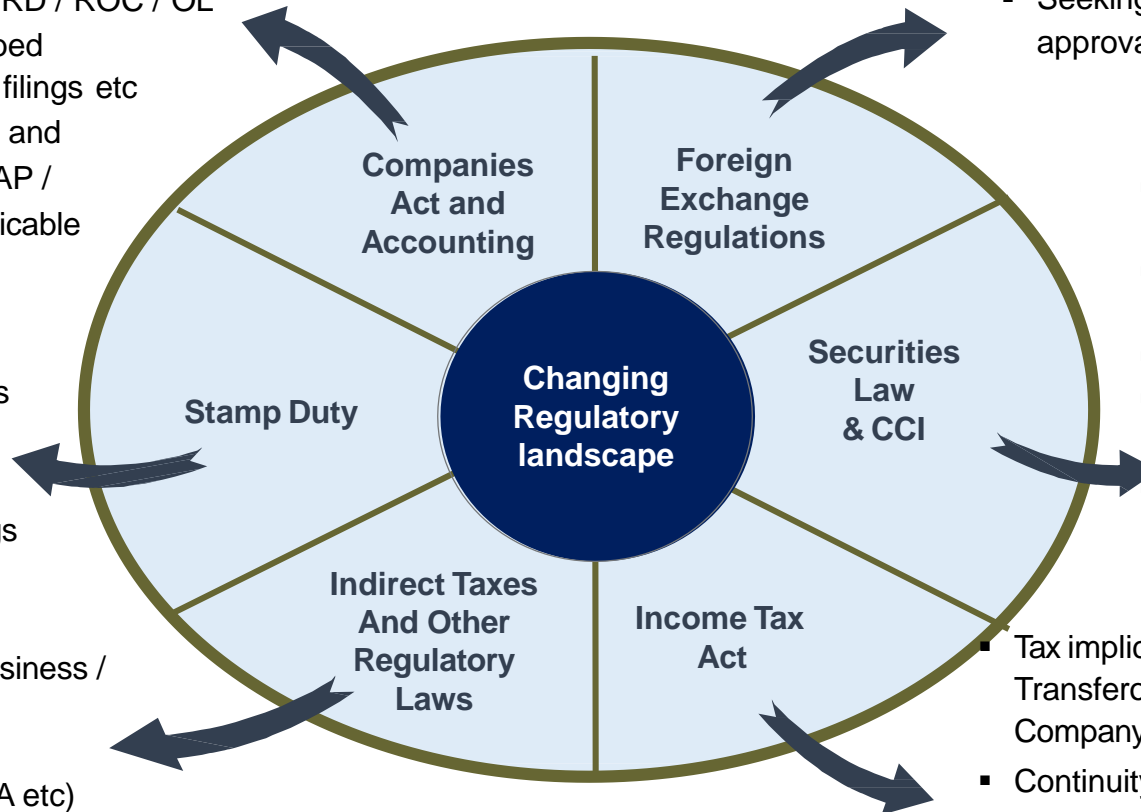
# M&A Framework



- Scheme of arrangements u/s 230 – 234 of the Companies Act, 2013
- Approvals from NCLT / RD / ROC / OL
- Complying with prescribed procedures, resolution, filings etc
- Accounting implications and disclosures under I-GAAP / Ind-AS, as may be applicable

- Understanding state specific stamp duty laws
- Planning levies/ registration charges
- Adjudication proceedings etc.

- GST applicability on business / asset transfer
- Regulatory approvals, if applicable (Mining, IRDA etc)



- FDI/ ODI implications, Cross Border Merger implications etc.
- Seeking necessary RBI approvals

- Compliance with SEBI Regulations/approvals
- Stock exchange approvals
- Listing of shares
- Takeover code implications
- Approval of CCI for Combinations

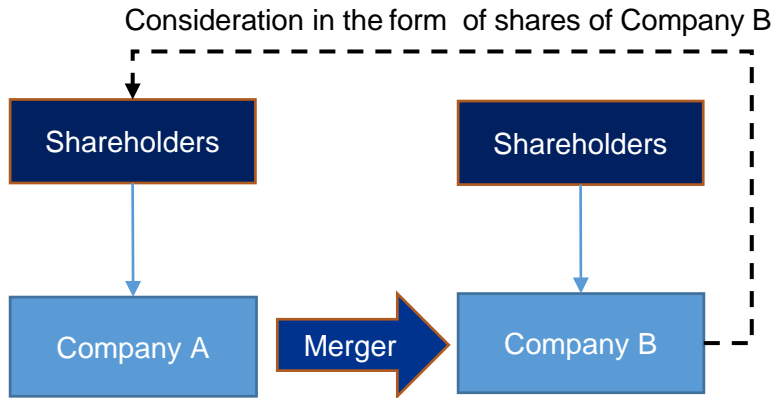
- Tax implications in the hands of the Transferor Company, Transferee Company and Shareholders
- Continuity of carry forward of losses
- Tax neutrality of restructuring and continuity of fiscal benefits

Most of the above have undergone a change in the recent times resulting into increased time frame for understanding and decision making

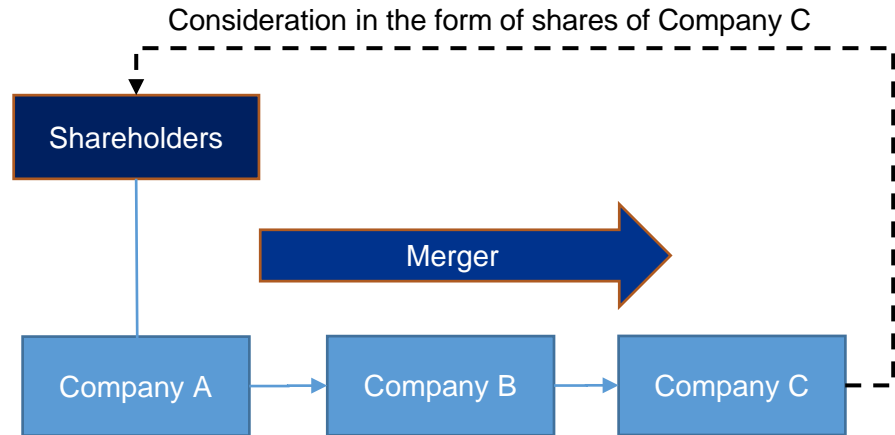
# Merger



# Merger - Typical Ways

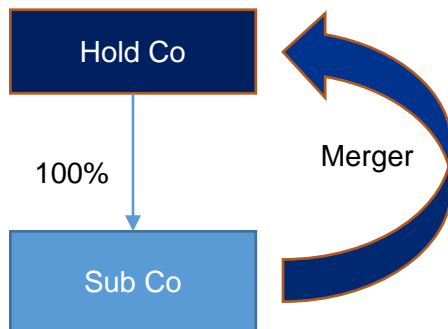


***Merger of Company A with Company B***



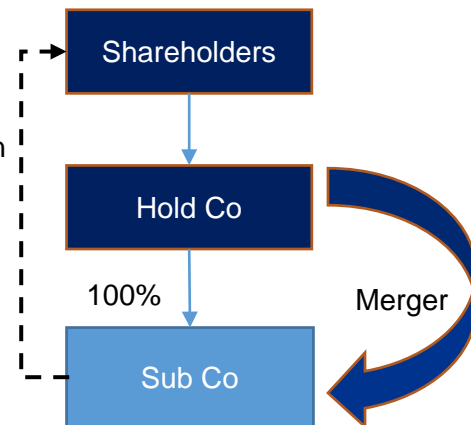
***Merger of Companies A & B with Company C***

No shares to be issued by Hold Co



***Merger of Sub Co with Hold Co***

Consideration in the form of shares of Sub Co



***Merger of Hold Co with Sub Co***

# Merger - Tax consideration



## **Section 2(1B) - "Amalgamation"**

- Merger of one or more companies with another company; or
- Merger of two or more companies to form one company

Conditions to be  
satisfied for tax  
neutral  
amalgamation  
[Section 2(1B)]

- Transfer of **all properties & liabilities** by the amalgamating company to the amalgamated company;
- Issue of shares to the shareholders holding not less than **3/4<sup>th</sup> shares (in value)** in the amalgamating company (***other than the shares already held by the amalgamated company or its nominees or its subsidiary***)

Merger of WOS into Holding Company

Tax neutral merger even though shares are not issued to the shareholders of amalgamating company

# Merger - Tax consideration



In the hands of	Taxability / Treatment	Section	Conditions
Amalgamating company	No capital gains tax on transfer of assets	47(vi)	Amalgamated company should be an Indian company
Shareholders of Amalgamating Company	No capital gains tax on transfer of shares	47(vii)	<ol style="list-style-type: none"> <li>1. Consideration to be <b><i>in form of shares in amalgamated company</i></b> (except where the amalgamated company itself is a shareholder)</li> <li>2. Amalgamated company should be an Indian company</li> </ol>
Cost of acquisition of shares received on amalgamation by the shareholders	= Cost of acquisition of shares held by the shareholders in the amalgamating company	49(2)	Transfer as referred u/s. 47(vii)
Period of holding of shares received on amalgamation by the shareholders	Includes period of holding of shares held by the shareholders in the amalgamating company	Expln. (i)(c) to 2(42A)	Transfer as referred u/s. 47(vii)

# Merger - Tax consideration



In the hands of	Taxability / Treatment	Section	Conditions
Cost of Assets for Amalgamated Company: - Stock - Capital Assets - Depreciable Assets	= Cost of acquisition of the stock / capital assets to the amalgamating company = WDV of depreciable assets held by amalgamating company	- 43C - Expln. 7 to 43(1) - 49(1) - Expl. 2 to 43(6)(c)	Amalgamated company should be an Indian company
Period of holding of capital assets received by Amalgamated company pursuant to amalgamation	Includes period for which capital assets were held by the amalgamating company	Expln. (i)(b) to 2(42A) r.w.s. 49(1) and 47(vi)	

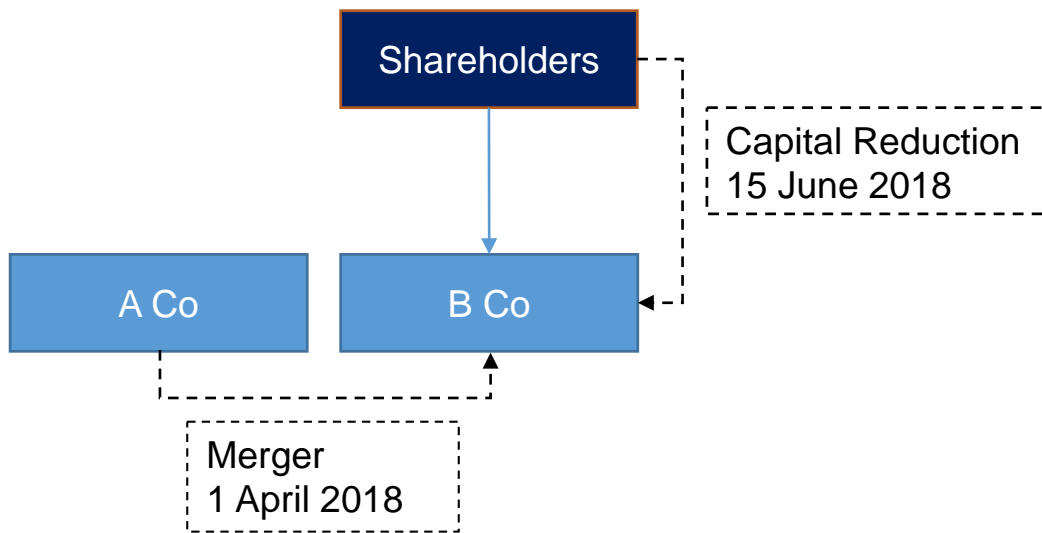


# Impact of Explanation 2A of section 2(22)



## Explanation 2A of section 2(22)

- In case of an amalgamated company, the accumulated profits, whether capitalized or not, or loss, as the case may be, shall be increased by the accumulated profits, whether capitalized or not, of the amalgamating company on **the date of amalgamation**



Particulars	INR
Accumulated Profit of A Co	150
Accumulated Profit of B Co	50
<b>Total</b>	<b>200</b>

Accumulated profit for capital reduction

What if the merger had happened in 2016? Can accumulated profits of A Co. be considered at the time of capital reduction?

# Key points to be consider under Income tax



Whether merger falls within the definition as per Section 2(1B)

Discharge of consideration by way of mix of equity and debenture or cash

Merger of holding company with wholly owned subsidiary company?

Goodwill created upon amalgamation and its tax treatment

Transfer of MAT credit upon amalgamation

Availability of business losses and unabsorbed depreciation

Whether 56(2)(viib) applies in case of issue of shares pursuant to merger?

# Merger - Carry forward of Business Losses and Unabsorbed Depreciation



## Section 72A

Accumulated business loss and unabsorbed depreciation of the amalgamating company shall be **deemed to be business losses or unabsorbed depreciation (as the case may be) of the amalgamated company for the previous year in which the amalgamation is effected**

## Should be in the business for carry forward of losses and UAD

- a company owning an industrial undertaking or a ship or a hotel with another company;
- a banking company with a specified bank;
- one or more public sector company or companies engaged in the business of operation of aircraft with one or more public sector company or companies engaged in similar business

Whether fresh lease of life will be available for carry forward of business losses in case of amalgamation?

# Carry forward of Business Losses and Unabsorbed Depreciation



## Industrial Undertaking

means any undertaking which is engaged in -

- the manufacture or processing of goods; or
- the manufacture of computer software; or
- the business of generation or distribution of electricity or any other form of power; or
- the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services; or
- mining; or
- the construction of ships, aircrafts or rail systems;

## Conditions - Amalgamating company [Section 72A(2)(a)]

- has been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for three or more years;
- has held continuously as on the date of the amalgamation at least three-fourths of the book value of fixed assets held by it two years prior to the date of amalgamation;

# Carry forward of Business Losses and Unabsorbed Depreciation



## Conditions - Amalgamated company

[Section  
72A(2)(b) read  
with Rule 9C]

- holds continuously for a **minimum period of five years** from the date of amalgamation at least three-fourths of the book value of fixed assets of the amalgamating company acquired in a scheme of amalgamation;
- continues the business of the amalgamating company for a **minimum period of five years** from the date of amalgamation;
- which owns an industrial undertaking of the amalgamating company by way of amalgamation, shall achieve the level of production of **at least fifty per cent** of the installed capacity of the said undertaking **before the end of four years** from the date of amalgamation and continue to maintain the said minimum level of production **till the end of five years** from the date of amalgamation; (Central Government may relax this condition on an application made by the amalgamated company)
- to furnish to the Assessing officer a **certificate in Form No. 62**, duly verified by an accountant from the year of achieving fifty percent level of production up to completion of five years from the date of amalgamation

In case of violation of any conditions, the set off of business losses or unabsorbed depreciation made in any previous year in the hands of amalgamated company shall be deemed to be income of amalgamated company chargeable to tax for the year in which such conditions are not complied with

# Section 79 - Change in substantial shareholding



Impact on Losses due to change in substantial shareholding

Carry forward and set off of losses (incurred in any year prior to the year of change in shareholding) against future income (post change in shareholding) will be lost, if,

- there is change in shareholding of a **company (not being a company in which public are substantially interested)**;
- shareholders beneficially holding **not less than fifty-one percent** of the voting power on the **last day of the year(s) in which loss was incurred** are not the same shareholders beneficially holding shares carrying **not less than fifty-one percent** of the voting power on the **last day of the year of set-off**

Change in shareholding of an Indian company as a result of amalgamation / demerger of its foreign holding company

- No impact on carry forward and set off of losses subject to the condition that **fifty-one per cent** shareholders of the amalgamating or demerged foreign company continue to be the shareholders of the amalgamated or the resulting foreign company

If, within the same year, shareholding changes by more than 49% and subsequently, original shareholding is restored. Can provisions of section 79 trigger?

# Section 79 - Change in substantial shareholding



Change in shareholding in case of eligible start up companies as referred in section 80-IAC

- No loss incurred in any of the **seven year** beginning from the year of incorporation which is prior to the year of change shall be carried forward and set off against the income of the year of change,
- unless all the shareholders (in the year of incurring the loss) continue to hold shares in the start-up company

Exceptions to Section 79

- a company where a change in the shareholding takes place in a year pursuant to-
  - a resolution plan approved under the Insolvency and Bankruptcy Code, 2016;
  - the death of a shareholder;
  - transfer of shares by way of gift to any relative from the shareholder

Whether section 79 applies to all losses including unabsorbed depreciation?

Whether Section 72A overrides Section 79?

# Section 79 - Change in substantial shareholding



## Two schools of thoughts on applicability of Section 79 (legal ownership v/s. beneficial ownership)

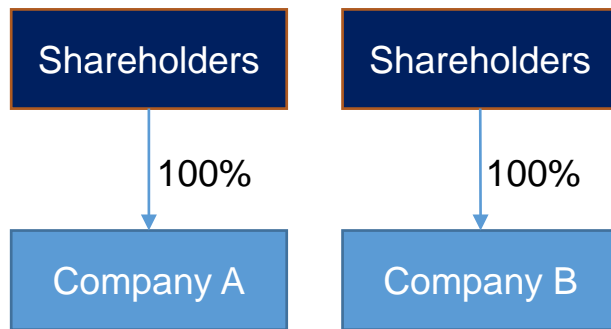
- Vital to analyse who is the legal owner of shares
  - A company is a distinct legal entity, and has an existence separate from that of its shareholders – assets of the company are not assets of the shareholders
  - A person can be a beneficial owner when shares are held by someone else on his behalf
  - Change in registered shareholder triggers section 79
  - Case laws:
    - Yum Restaurants (Delhi HC)
    - Acer Computer International Limited (AAR)
    - Tainwala Trading and Investments (ITAT Mumbai)
    - Just Lifestyle (ITAT Mumbai)
- Section 79 states that shares carrying not less than 51% of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than 51% of voting power on the last day of the year in which loss was incurred
  - A subsidiary is effectively controlled by its parent company; the parent company controls the voting power of the company
  - Section 79 is not triggered if the beneficial holders remain the same, even if there is change in the immediate shareholders
  - Case laws:
    - Amco Power Systems (ITAT Bangalore; upheld by Karnataka HC)
    - Select Holiday Resorts (ITAT Delhi)
    - Wadhwa & Asso. Realtors Pvt Ltd (ITAT Mumbai)



# Case Study

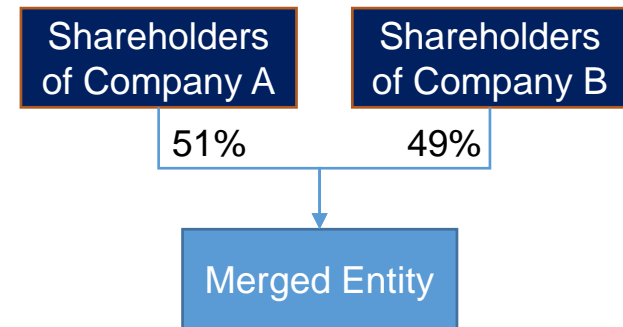


## Pre-amalgamation structure



Company A Losses – INR 100 crores  
Company B Losses – INR 200 crores

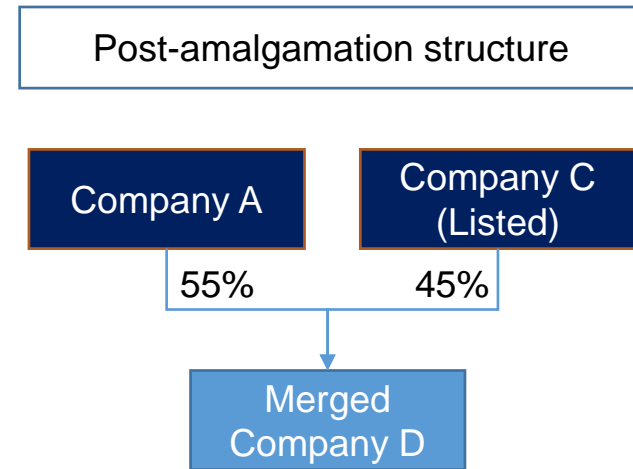
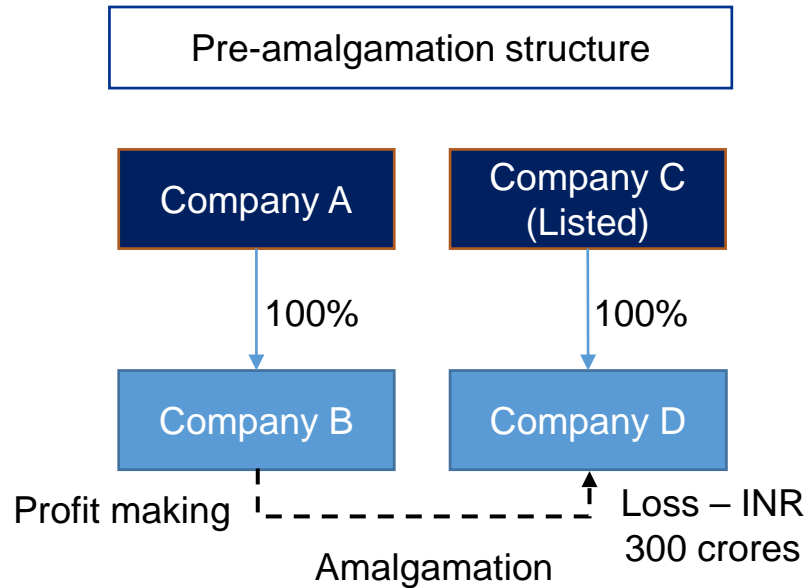
## Post-amalgamation structure



Will the losses be available to the merged entity in the following scenarios (Assuming Co. A and Co. B are industrial undertaking:-

- Company A merges with Company B
- Company B merges with Company A
- Company A and Company B merge to form New Co.

# Case Study

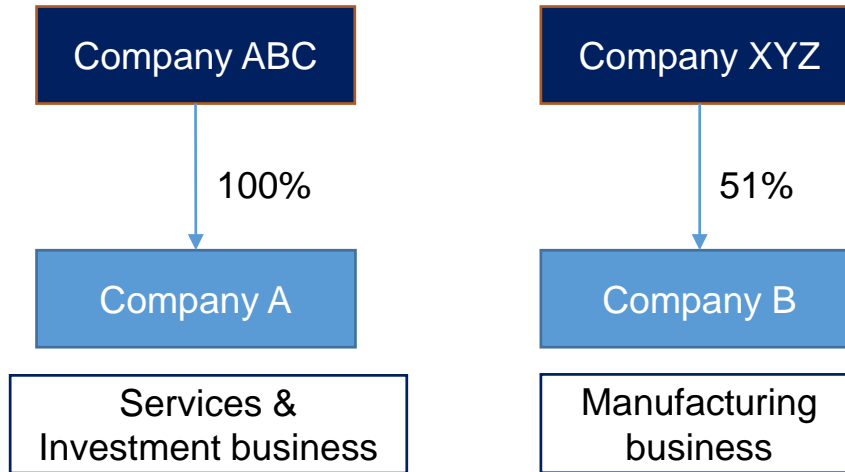


## Facts of the case:

- Company D is a manufacturing entity
- Company C is a listed company
- Proposal is to merge Company B into Company D

Whether losses can be carried forward by Company D ?

# Case Study



## Facts of the case:

- Company A is a closely held company & Company B is a Listed Company
- Company A has accumulated tax losses in service business
- Proposal is to consolidate Company A and Company B

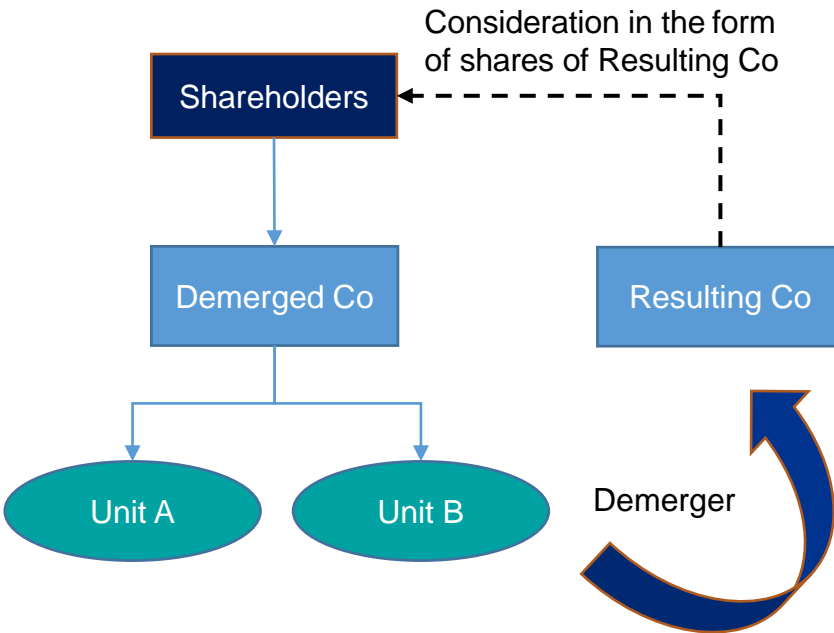
Will the losses be available to the merged entity in the following scenarios :-

- Merger of Company A with Company B
- Merger of Company B with Company A
- Demerger of service business of Company A into Company B

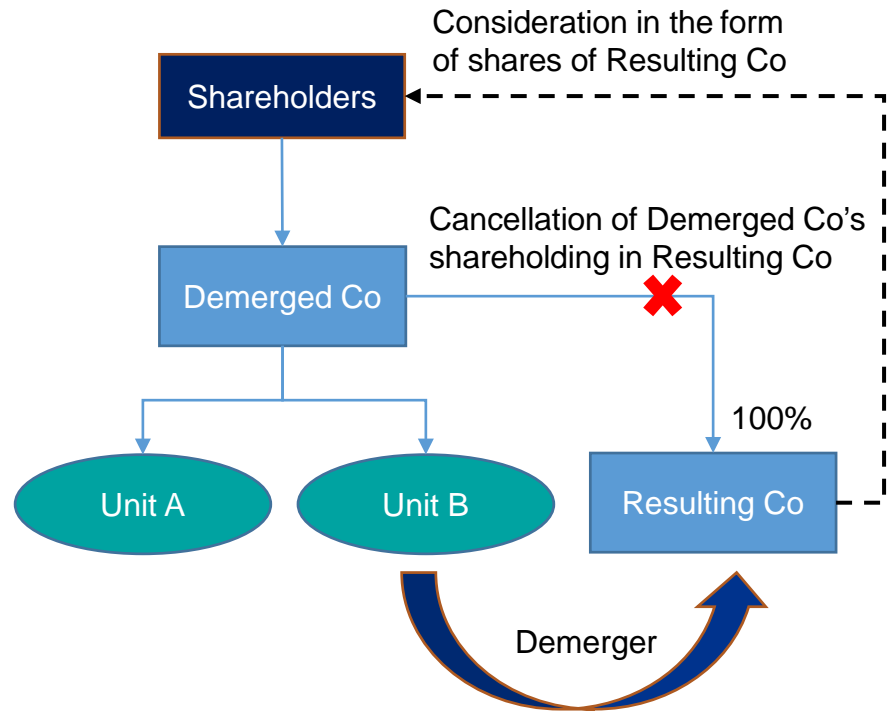
# Demerger



# Demerger - Modus operandi



***Non-Mirror shareholding Demerger***



***Mirror shareholding demerger – this is typically carried out by the listed company and pursuant to demerger the resulting company will also get listed***

# Demerger - Tax Consideration



## Meaning

“**Demerger**” means the transfer of one or more undertakings by the demerged company to any resulting company

## Conditions to be satisfied for tax neutral demerger [Section 2(19AA)]

- Transfer of all properties & liabilities relatable to the **undertaking** being transferred by the demerged company to the resulting company **at book value**;
- Discharge of consideration by the resulting company by way of **issue of shares on proportionate basis** (except where resulting company itself is a shareholder of the demerged company);
- Issue of shares to the shareholders holding **not less than 3/4<sup>th</sup> shares (in value)** in the demerged company (other than the shares already held by the resulting company or its nominees or its subsidiary);
- Transfer of undertaking to be on a going concern basis

## Undertaking

“**Undertaking**” shall include any part of an undertaking, or a unit or division of an undertaking or 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 1 to Section 2(19AA)]

# Demerger - Tax Consideration



## Demerged Company

“**Demerged company**” means the company whose undertaking is transferred to a resulting company pursuant to demerger [section 2(19AAA)]

## Resulting Company

[Section 2(41A)]

- “**Resulting company**” means one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and, the resulting company in consideration of such transfer of undertaking, issues shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger [section 2(41A)]

Whether wholly owned subsidiary includes step down wholly owned subsidiary also?



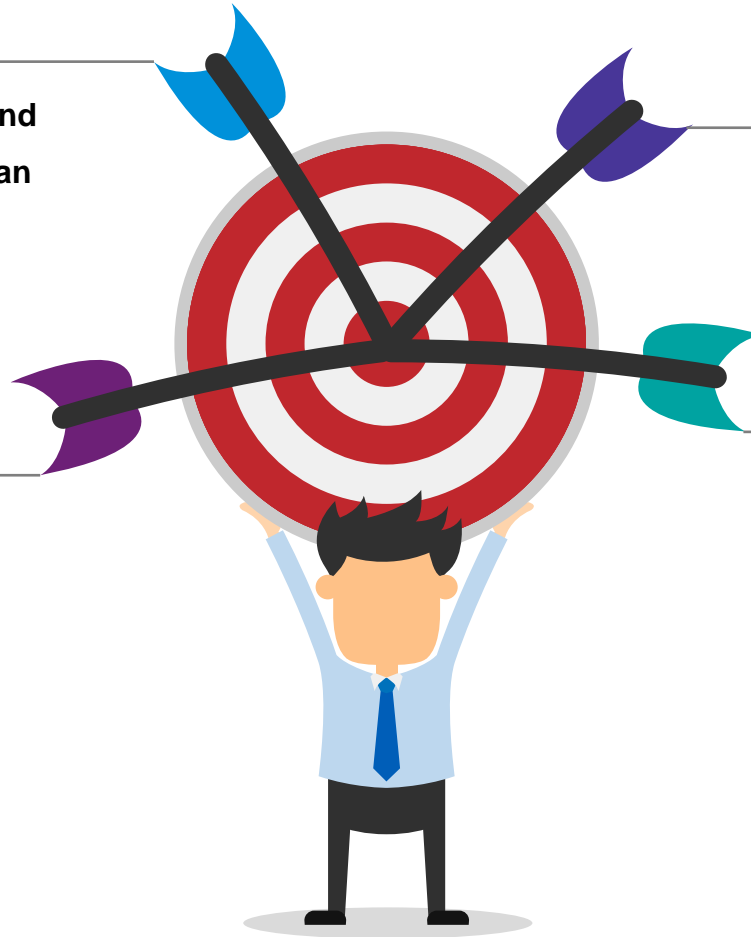
## Issues in relation to what constitutes an “Undertaking”

Can investments in shares and securities be considered as an undertaking?

Can a project under construction be considered as an undertaking?

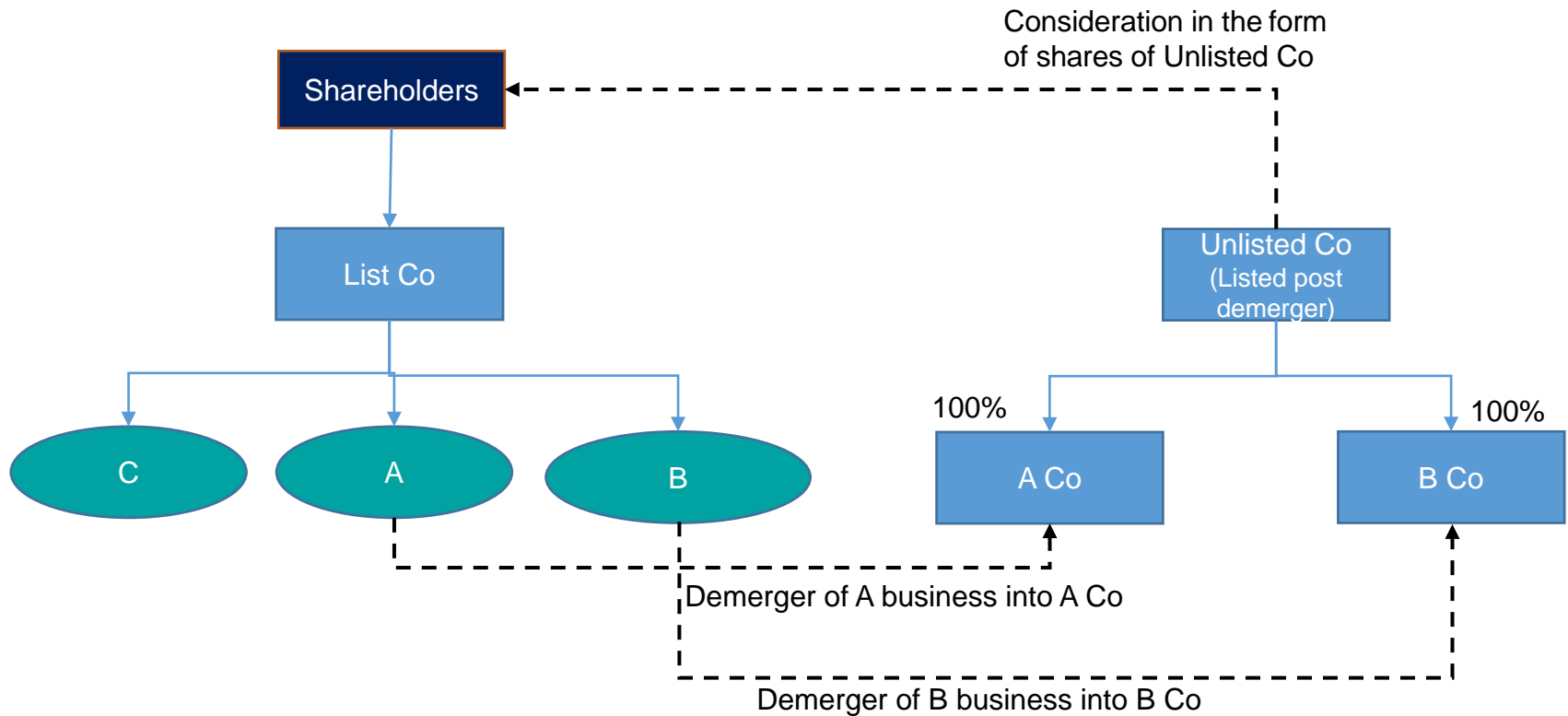
Can a company having only one undertaking, be demerged?

If certain common assets / back-office operations are not transferred, will it jeopardize the nature of undertaking?





# Recent Demerger - A Case Study



The undertakings were transferred to A Co and B Co but shares were issued by the holding company i.e. Unlisted Co under section 2(41A) of the IT Act

# Demerger – Tax Consideration



In the hands of	Taxability / Treatment	Section	Conditions / Remarks
Demerged Company	No capital gains tax on transfer of assets	47(vib)	Resulting company should be an Indian company
Shareholders of Demerged Company	No capital gains tax on receipt of shares from the resulting company	47(vid)	
Cost of Assets for Resulting Company: - Depreciable Assets - Capital Asset	= WDV of depreciable asset to be the same as WDV in the hands of the Demerged Company = No specific provision for cost of Capital Asset acquired	- Expln 7A to 43(1) - Expln 2B to 43(6)(c) - 49(1)	Resulting company should be an Indian company
Cost of acquisition of shares received on demerger by the shareholders	= Cost of acquisition of shares in demerged company be split on the basis of net book value of the assets transferred bearing to the Net worth of the Demerged Company immediately before such demerger	49(2C)	

# Demerger – Tax Consideration



In the hands of	Taxability / Treatment	Section	Conditions / Remarks
Period of holding of shares received on demerger by the shareholders	Includes period of holding of shares held in the demerged company	Explanation 1(i)(g) to Section 2(42A)	
Period of holding of capital assets	Includes period of holding of capital assets held by the demerged company	Expln 1(i)(b) to 2(42A) r.w.s. 49(1) and 47(vib)	

# Demerger - Tax Consideration



## Cost split up in the hands of shareholders

- **“Cost of acquisition of shares of resulting company”** [Section 49(2C)]

$$\begin{aligned} &= \text{Cost of acquisition of shares} && \text{Net book Value of the assets} \\ &\text{in demerged Company} && \text{transferred in the demerger} \\ & && \hline & && \text{Net worth of the demerged} \\ & && \text{company before the demerger} \end{aligned}$$

- **“Cost of acquisition of the original shares held by the shareholders in the demerged company”** [Section 49(2D)]

= Cost of acquisition of shares in demerged company – cost of acquisition of shares of resulting company arrived at under section 49(2C)

- **“Net worth”** is defined as the aggregate of the paid up share capital and general reserves as appearing in the books of account of the demerged company immediately before the demerger

Whether the definition of Net worth is to be interpreted strictly to includes only ‘General Reserve’?

How to compute the cost split in case of demerger of negative network undertaking?

# Demerger - Carry forward of Business Losses and Unabsorbed Depreciation



Where accumulated business losses and unabsorbed depreciation are directly relatable to the undertaking demerged  
[Section 72A(4)(a)]



Entire amount of directly relatable business losses and unabsorbed depreciation is allowed to be carried forward and set off in the hands of the resulting company

Where accumulated business losses and unabsorbed depreciation are not directly relatable to the undertaking demerged  
[Section 72A(4)(b)]



The accumulated business loss and unabsorbed depreciation should be apportioned between the resulting company and the demerged company **in the ratio of the assets transferred to the resulting company and assets retained by the demerged company** and be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be

Whether fresh lease of life will be available for carry forward of business losses in case of demerger?

# Tax Incentives and MAT Credit



## Tax Holidays

- Tax Incentives are either based on business (u/s 80-IA/80-IB/10B) or Area/ Region based (u/s. 80-IC/10A/ 10C)
- Continuity of unexpired period of tax holiday to the transferee company in amalgamation / demerger except\_u/s. 80-IA(12A)
- Availability of above tax holiday in case of Slump sale is a matter of litigation

## MAT Credit

- MAT payable on book profits in the absence of Nil / lower tax profits
- Credit for MAT allowable to the assessee company who has paid such taxes
- Amalgamating company ceases to exist after amalgamation
- No specific provision in the IT Act for carry forward of MAT credit in case of amalgamation or demerger. However, Mumbai ITAT\* and Ahmedabad ITAT\*\* have endorsed a favorable view in case of amalgamation and demerger (proportionate basis) respectively

## Section 56

- No implications on receipt of properties in the hands of the Transferee Company pursuant to amalgamation or demerger - Clause (IX) to the proviso of Section 56(2)(x)

\* SKOL Breweries Ltd vs ACIT [2008] 28 ITATINDIA 998 (Mum)

\*\* Adani Gas Ltd. v. ACIT (ITA Nos. 2241 & 2516/Ahd/2011)

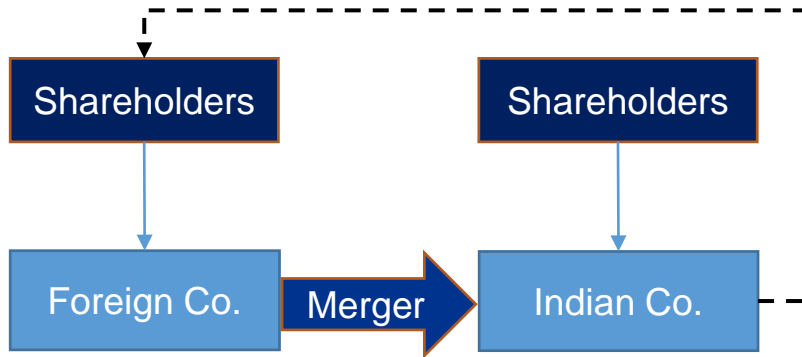
# Cross border merger



# Cross Border Merger

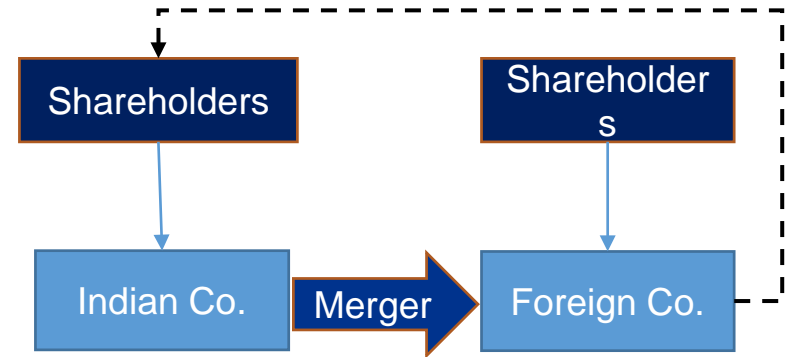


Consideration in the form of shares of Indian Co.



Inbound Mergers are mergers wherein a foreign company merges with an Indian company

Consideration in the form of shares of Foreign Co.



Outbound Mergers are mergers wherein an Indian company merges with a foreign company



# Challenges in Cross Border Merger

*still some path to cross...*



## Inbound Merger

## Outbound Merger

Treatment of accumulated losses of foreign company

Income-tax exemption not available

Non FEMA compliant assets and liabilities needs to be addressed within 2 years

Issue of shares to resident only up to LRS

Round tripping issue

Permanent Establishment risk

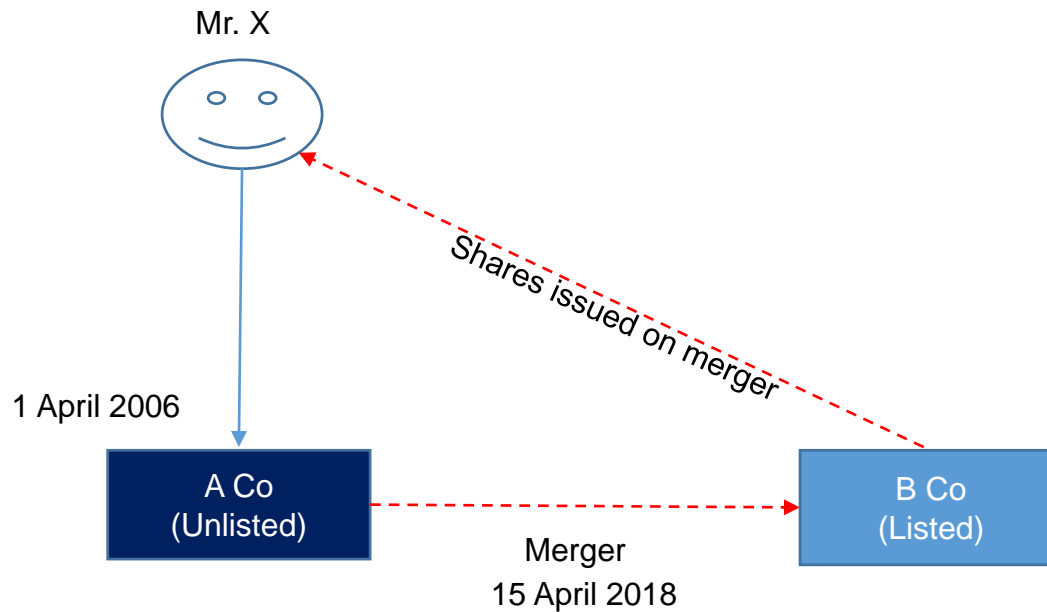
# Case studies



# Case study



Merger of A Co (Unlisted) into B Co (Listed Co) and Mr. X issued listed shares of B Co

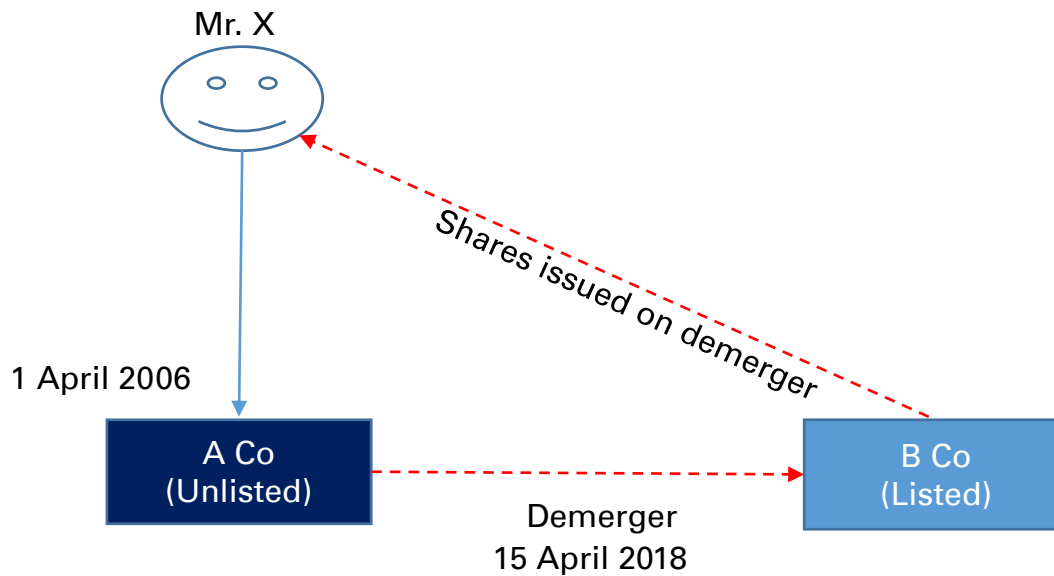


What will be the cost of acquisition of B Co.'s shares in the hands of Mr. X ?

# Case study



## Demerger of A Co (Unlisted) into B Co (Listed Co)

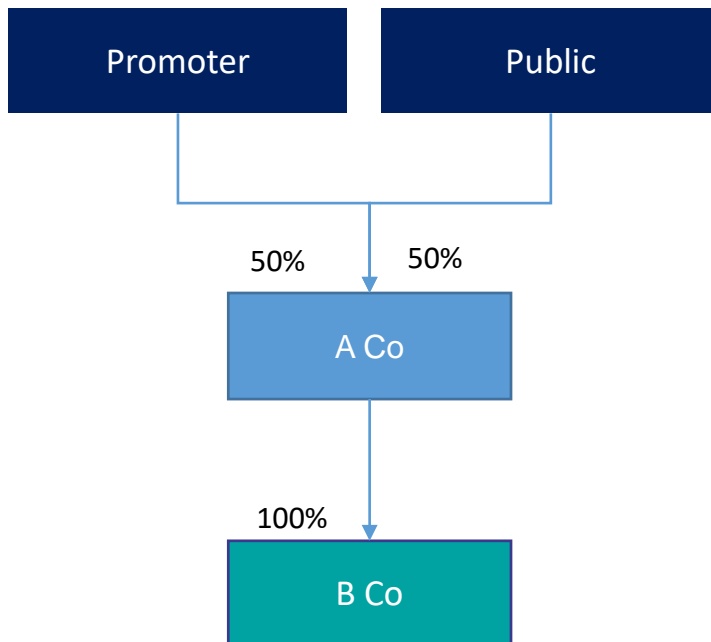


How the cost of acquisition of shares of B Co. in the hands of Mr. X would be computed?

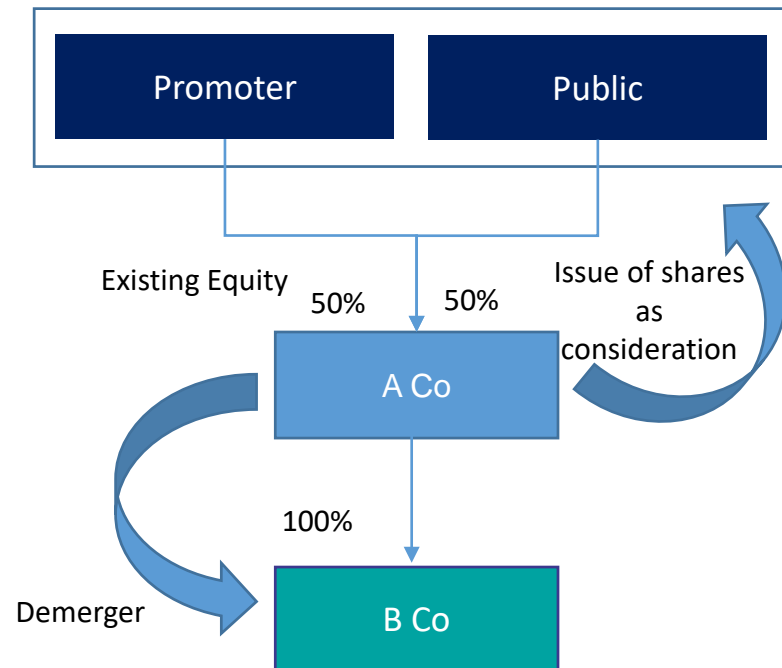
# Case study



## Current Structure

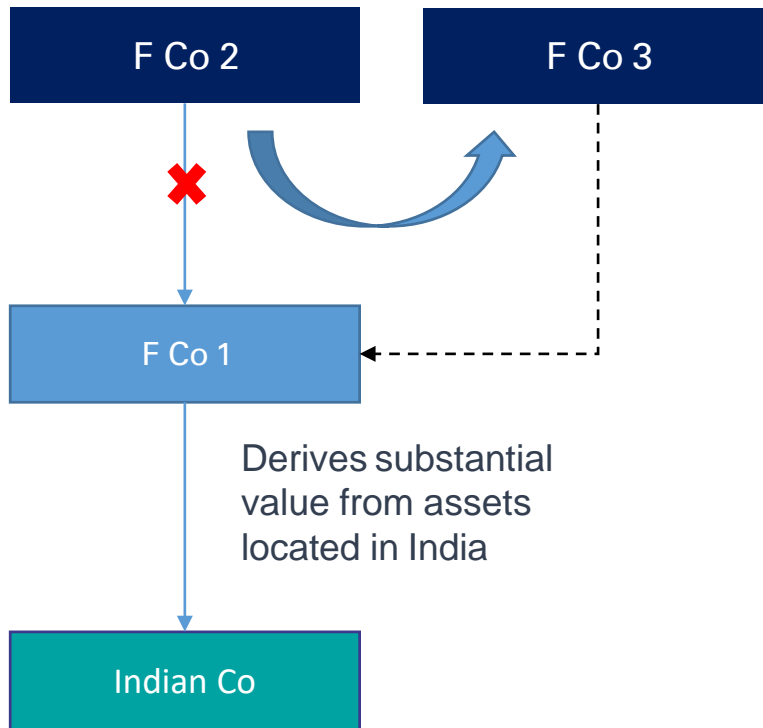


## Proposed Structure



Whether demerged company and resulting can be the same company?

# Case study



## Consider the following scenario:

- F Co 1 holds 100% in Indian Co
- F Co 2 holds 100% in F Co 1
- F Co 2 to merge into F Co 3
- Transfer of shares of F Co 1 to F Co 3 upon merger

What will be the tax implications in India?

# Buy-back



# Buy-back of Shares



## Taxability provisions

[Section 115QA]

- From 1 June 2013, Buyback tax provisions were introduced on unlisted companies and exemption was provided to its shareholders, as buy-back tax was to be paid by the company
- Currently, buy-back of shares is taxable @ 23.296% on the difference between buy-back consideration and amount which was received by the company for issue of such shares
- Buy-back provisions are not applicable to listed companies so gains on buy-back, if any, are taxable in hands of shareholder of the listed company

## Other provisions

- In case of corporate shareholders, MAT may be applicable
- No deemed dividend implications on buyback [*Clause (iv) to section 2(22)*]
- The provision of buy-back tax have not dealt with the following:
  - Allowability of any expenses incurred during the buy-back of shares
  - Indexation benefit available to shareholders in case of normal sale of shares instead of buy-back
  - Redemption of RPS – whether buy-back tax applies?



# Buy-back of Shares



Taxability in the hands of	Listed Shares				Unlisted Shares	
	Buyback through Stock Exchange Mechanism (subject to STT)		Buyback directly from Shareholders (Not subject to STT)			
	Equity Shares	Preference Shares	Equity Shares	Preference Shares	Equity Shares	Preference Shares
<b>Company</b>						
Liability of Buyback Tax	No	No	No	No	Yes	Yes
<b>Shareholders</b>						
Held more than 12 months (listed shares) / 24 months (unlisted shares) *	10% (gains exceeding INR 1 lakh)	20% (with indexation) 10% (without indexation)		Exempt u/s 10(34A)		
Held upto 12 months (listed shares) / 24 months (unlisted shares) *	15%	As per slab rates				

\* Plus applicable surcharge and cess

# Capital reduction



# Capital Reduction of Shares



## Tax implications in the hands of the company

- Distribution to shareholders by a Company on the reduction of its capital is deemed as dividend to the extent to which the Company possesses accumulated profits, whether capitalized or not
- Deemed dividend u/s 2(22)(d) is subject to Dividend Distribution Tax u/s 115-O of the IT Act

## Tax implications in the hands of the shareholders

- Reduction of share capital by a company and pro-rata distribution of cash / assets to the shareholders amount to transfer and therefore, taxable as capital gains
- For determining the amount liable to capital gain tax, full value of consideration is reduced by the amount, which has been reckoned as dividend

## Other provisions

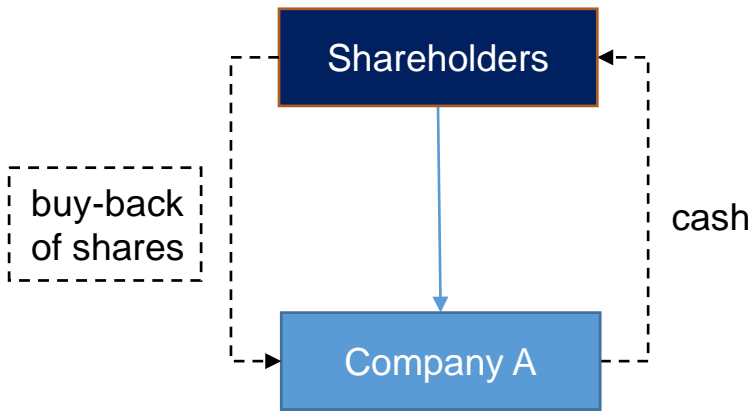
- Capital loss on account of capital reduction in the hands of the shareholders not involving payment of any consideration cannot be allowed under the provisions of IT Act. [*Bennett Coleman & Co. Ltd. v. The Addl. CIT (ITA No 3013/MUM/2007)*]
- Applicability of Section 56(2)(x) provisions

# Impact of Section 50CA



- Section 50CA, as introduced by the Finance Act 2017, provides for **adoption of FMV (as prescribed in Rule 11UAA) as the consideration for transfer of unquoted shares of a company, where actual consideration is lower than FMV**
- The difference between FMV and consideration shall be subject to tax in the hands of the transferor under the head “Capital gains”
- Applicable to transferor who holds shares as capital asset and not as stock-in-trade
- Extends to any form of shares whether equity or preference. But does not cover convertible debt instrument such as CCD or warrants or right entitlement
- Transactions which are not likely to be covered by section 50CA include:
  - Capital reduction with no consideration
  - Transfer by way of gift which is exempted under section 47(iii)
  - Any transfer which can qualify for exemption under section 47 or under the treaty
- Section 50CA is different from section 50D as taxation under section 50D is triggered only when consideration is unascertainable while section 50CA is in respect of ascertained consideration which is less than prescribed FMV

# Case Study

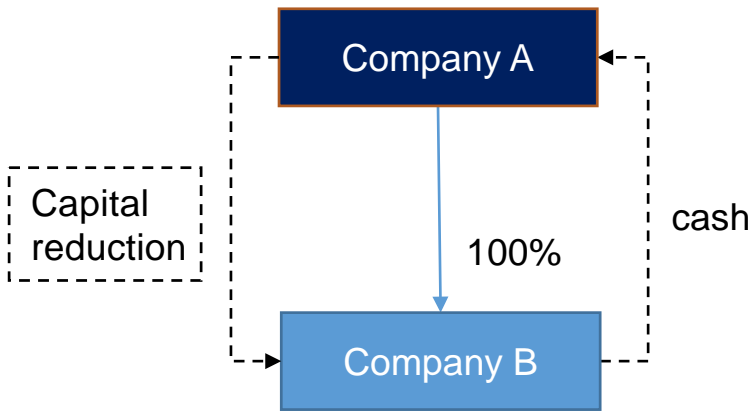


## Facts of the case:

- Company A, an Indian unlisted company, undertakes buy back of its own shares
- Company A to buy back 20 lakh shares at Rs. 100/share. Fair market value of the same is Rs. 120/share
- Company A to pay cash as a consideration to the shareholders whose shares are being bought back

Will there be any tax implication u/s. 56(2)(x) of the IT Act in the hands of Company A?

# Case Study

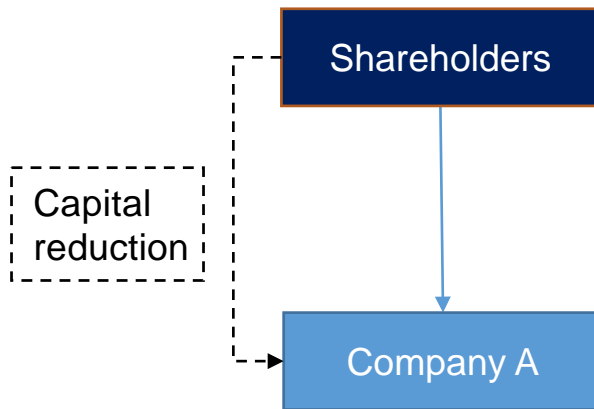


## Facts of the case:

- Company B is wholly owned subsidiary of Company A
- Company B, an Indian company, undertakes capital reduction
- Company B to pay cash as a consideration to the shareholders

Can Company A claim exemption u/s. 47(iv) of IT Act?

# Case Study

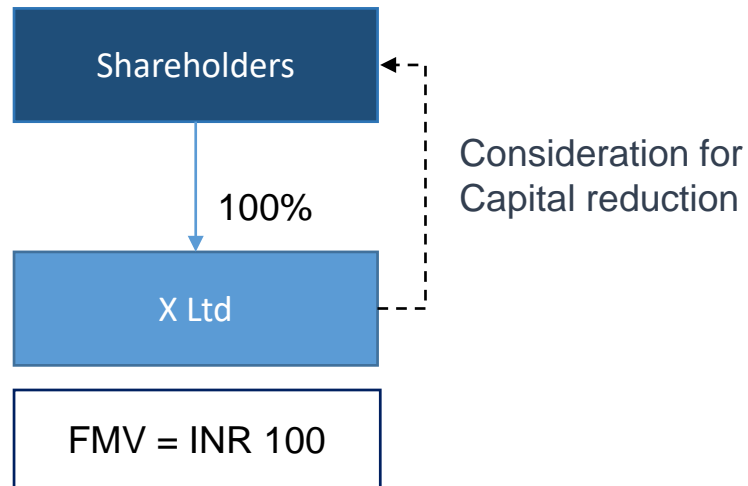


## Facts of the case:

- Company A, an Indian company, undertakes capital reduction against accumulated losses of the company and no cash is paid on capital reduction to the shareholders

What will be the taxability of loss on capital reduction in the hands of the shareholders?

# Case Study



Whether Section 50CA applies in any of the below scenarios?

- Consideration paid on capital reduction is INR 150
- Consideration paid on capital reduction is INR 40
- Capital reduction is done at par value
- Capital reduction is done at NIL value



# Slump Sale



# Slump Sale



## Meaning of Slump Sale [Section 2(42C)]

- the transfer of one or more **undertakings**
- as a result of sale for a **lump sum consideration**
- **without values being assigned to individual assets and liabilities** in such sales
- Explanation - Determination of value of an asset or liability for the sole purpose of payment of stamp duty, registration fees or other similar taxes or fees shall not be regarded as assignment of values to individual assets or liabilities

## Undertaking

**“Undertaking”** shall include any part of an undertaking, or a unit or division of an undertaking or 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 1 to Section 2(19AA)]

## Capital Gains in the hands of the Seller [Section 50B]

- Capital Gains = Consideration less Net Worth (deemed COA) of Undertaking
- No indexation benefit will be available
- Net worth = Aggregate value of total assets of the undertaking - Book value of liabilities of such undertaking
- Value of total assets = Tax WDV of depreciable assets + Book value of other assets
- Capital Gains will be classified as long-term, if undertaking is held for more than 3 years



## Cost allocation

- How should the consideration be allocated ?

## Section 281

- Whether slump sale is covered under Section 281?
- Transfer shall be not be void if it is made:
  - for adequate consideration **and** without notice of pendency of proceedings or, as the case may be, without notice of such tax or other sum payable by the assessee; or
  - with the previous permission of the Assessing Officer

## Section 170

- Whether Section 170 covers slump sale?
- Predecessor (Seller) to be assessed in respect of the income of the previous year upto the date of succession (transfer)
- The Successor (buyer) would be assessed if the predecessor cannot be found with respect to the income of the previous year upto the date of succession

# Section 50B vs Section 50C and Section 43CA



## Transfer of an “Undertaking” by way of sale includes land, building or both

- **Whether covered under section 50B or section 50C or section 43CA?**

- **Section 50B – Special provision for computation of capital gains in case of slump sale**

- In slump sale, capital asset which is the subject matter of charge, is the ‘Undertaking’ and not the land and building which make up that undertaking
- No identifiable consideration received or accrues as a result of the transfer of land or building. Hence, not possible to determine whether any consideration received or accruing is attributable to land or building
- Explanation to section 2(42C)

- **Section 50C – Special provision for full value of consideration in certain cases**

- Capital asset subject matter to charge, is the land or building or both which must be transferred
- Consideration must have been received or accrued as a result of such transfer which must be less than stamp duty valuation - Capital gains to be computed in accordance with section 48
- In such a case, stamp duty valuation of such capital asset shall be deemed as the full value of consideration

# Section 50B vs Section 50C and Section 43CA



- **Section 43CA – Special provision for full value of consideration for transfer of assets other than capital assets in certain cases**
  - The transfer of land or building or both held in the nature of stock in trade
  - Consideration must have been received or accrued as a result of such transfer which must be less than stamp duty valuation
  - Section 43CA is analogous to section 50C
  - In such a case, stamp duty valuation of such assets shall be deemed as the full value of consideration

In light of the above, possible to take a view that Section 50B overrides Section 50C and Section 43CA

# Itemized sale



# Itemized Sale



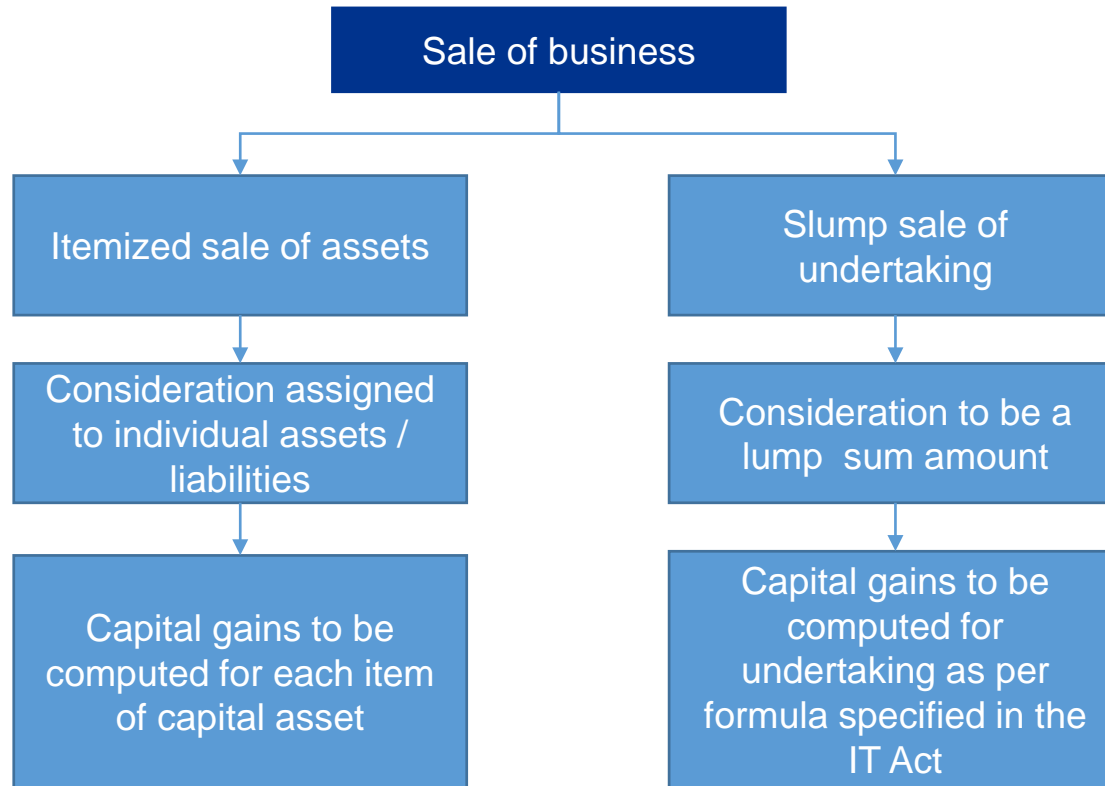
## Meaning of Itemized Sale

- Not defined under IT Act
- Involves individual sale of assets
- Consideration is identifiable against each asset
- Buyer discharges consideration to the seller for the asset acquired

## Tax Implications

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

# Itemized Sale vs Slump Sale





# Itemized Sale vs 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"> <li>– For depreciable assets – Short term</li> <li>– For non-depreciable assets – Depends on the period of holding of assets</li> </ul>	<ul style="list-style-type: none"> <li>– Depends on the period of holding of the undertaking</li> <li>– Holding period of individual assets not relevant</li> </ul>
Indexation benefit	Available (in case of non depreciable 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

# Key regulatory provisions governing mergers and demergers

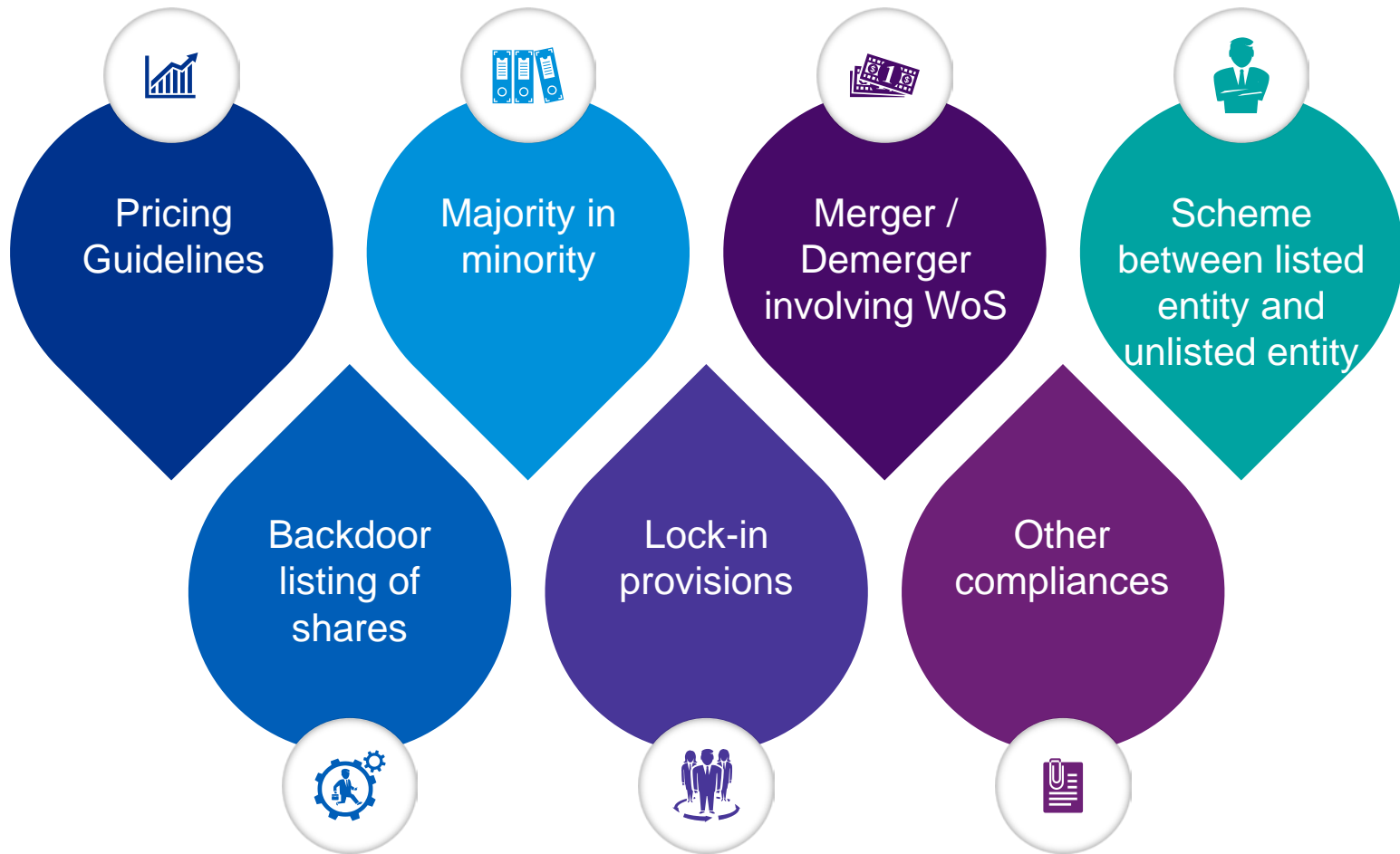


# SEBI / Stock Exchanges (only if listed company is involved)



- Listed Entities to comply with **Regulation 11, 37 and 94** of LODR for every Scheme of Arrangement proposed u/s 230 to 234 and Section 66 of CA 2013
- SEBI Circular dated March 10, 2017 (*as amended*) provides conditions and compliances by Listed Entities while undertaking Scheme of Arrangement
- Filing of Scheme of Arrangement by Listed Entities with NCLT only post receipt of observation letter or No objection letter (“Letter”) from SEs
  - Such Letter to be placed before Tribunal
  - Validity of Letter is 6 months from date of its issue
  - Submission of prescribed documents with SEs post sanction of Scheme

# Key pointers in SEBI Circular for Merger and Demergers





- Amalgamation / Demerger is regulated under section 230 to 234 of the Companies Act, 2013
- Approval of NCLT, MCA, RD, OL, other applicable authority will be required
- One of the most important documents in the process is the Scheme of Amalgamation / Arrangement
- Apart from others, following clauses in the scheme requires specific attention :
  - Vesting of Assets and Liabilities
  - Consideration
  - Appointed date and Effective date
  - Accounting treatment
  - Conditionality



Finalizing the scheme of amalgamation / arrangement and other relevant documents



Board meetings & Audit committee meetings (as applicable) of all the companies



Filing of the scheme with the Stock Exchanges (in case of listed companies) and other regulators (as may be applicable)



Obtaining No-Objection Certificate from the Stock Exchanges and approvals from other regulators (as may be applicable)



Filing applications with NCLT



Hearing of the applications by the NCLT and NCLT shall give directions to convene the meeting of shareholders and creditors and to issue notices to regulatory authorities



Shareholders and creditors meeting and issuing notices to regulatory authorities



Obtaining regulatory approval like RD, RoC, OL, etc. (as may be applicable)



Filing petition



Admission of petition



Final hearing at NCLT



Filing Order with ROC



## Stamp Duty implications on Merger / Amalgamation and Demerger

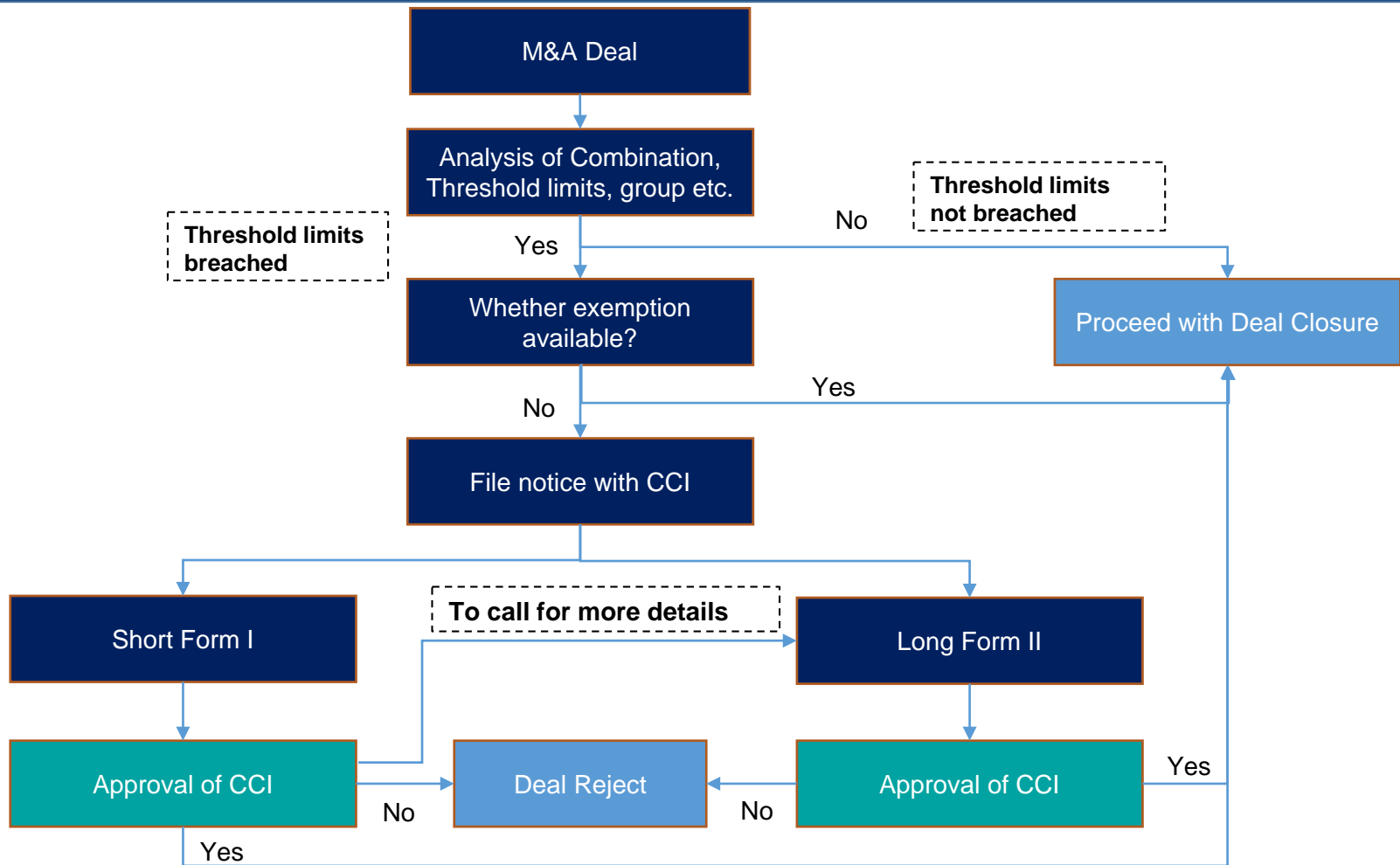
- Duty is payable in the States—
  - where order approving the scheme is passed; and
  - where the properties of transferor company are located
- Specific entry in the Schedule levying duty on NCLT order sanctioning amalgamation - *Maharashtra, Gujarat, Rajasthan, Haryana Karnataka, Andhra Pradesh*
- Applicability of 1937 Notification (Exemption of stamp duty on transfer of properties between parent and subsidiary company) – vary from state to state
- No specific entry in case of states other than the above
  - Depending on the state, possibility of mitigation of stamp duty could be explored through appropriate transfer mechanism



# Competition Laws



## Process Chart



Thank You