Corporate Restructuring -Amalgamation & Demerger

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Contents

- Meaning-Corporate restructuring;
- Different laws governing CR
- Company law implications;
- Accounting Standard;
- Income tax Act;
- Case Studies

Business Growth

- There are primarily two ways of growth of business organization, i.e. organic and inorganic growth.

- **Organic growth** is through internal strategies, which may relate to business or financial restructuring within the organization that results in enhanced customer base, higher sales, increased revenue, without resulting in change of corporate entity..

- **Inorganic growth** provides an organization with an avenue for attaining accelerated growth enabling it to skip few steps on the growth ladder. Restructuring through mergers, amalgamations etc constitute one of the most important methods for securing inorganic growth

Meaning of Corporate Restructuring

- Restructuring as per Oxford dictionary means “to give a new structure to, rebuild or rearrange".

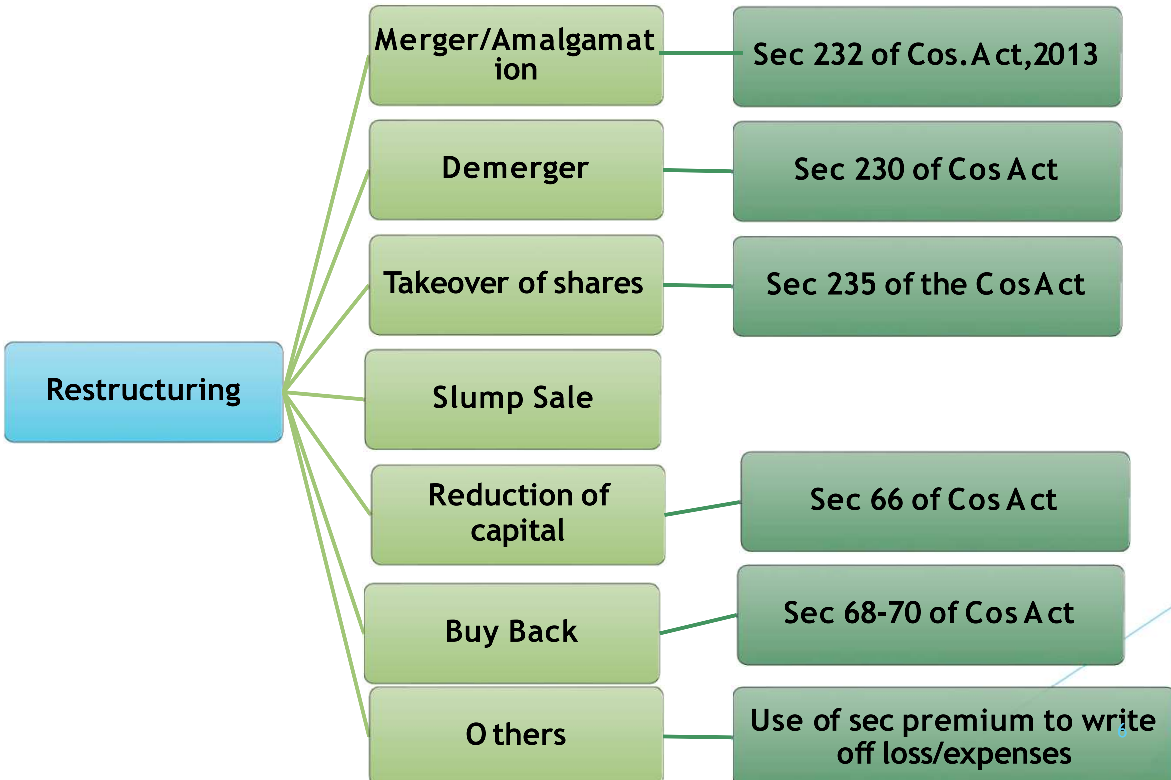
- As per Collins English dictionary, corporate restructuring is a change in the business strategy of an organization resulting in diversification, closing parts of the business, etc, to increase its long-term profitability.

- Corporate restructuring is defined as the process involved in changing the organization of a business.
- Corporate restructuring can involve making dramatic changes to a business by cutting out or merging departments. It implies rearranging the business for increased efficiency and profitability. In other words, it is a comprehensive process, by which a company can consolidate its business operations and strengthen its position for achieving corporate objectives-synergies and continuing as competitive and successful entity.

Why Corporate Restructuring

- Companies worldwide are refocusing, downsizing and merging to become globally competitive.
- Developing core competence for global /domestic competition, technological development through collaboration and joint venture
- Divesting non profitable business
- Closing down non operating companies
- It is an expression that connotes a restructuring process undertaken by business enterprises for the purpose of bringing about a change for the better and to make the business competitive.

Modes of Corporate Restructuring



Mergers, Demergers and Amalgamations-
An Overview

WHAT IS DEMERGER or AMALGAMATION?

Any thoughts???

What Is Merger/ Amalgamation/ Demerger?

- Not defined under the Companies Act, 1956
- ***What is defined under Companies Act, 2013?***
  - ***Arrangement-*** includes a re-organisation of the share capital of the company by the consolidation of shares of different classes, or by the division of shares into shares of different classes or, by both those methods
- ***What is defined under Income Tax Act?***
  - ***Amalgamation*** *[sec.2(1B)]*
  - ***Demerger*** *[2(19AA)]*

- **Meaning of the terms in common parlance:**
  - ***Amalgamation*** - combination of two or more independent business corporations into a single enterprise
  - ***Demerger*** – transfer and vesting of an undertaking of a company into another company

Regulatory Framework

- Companies Act, 2013– [Sec 230-236]- read Companies (Compromise, Arrangement and Amalgamation), Rules, 2016
- Accounting Standard – 14/ Ind-AS 103
- SEBI (Listing Obligation and Disclosure Requirements), 2015- Reg 11, 37 and 94
- SEBI Circular on Schemes of Arrangement- 10th March, 2017 r/w Amendments
- SEBI Takeover Code (in case of acquisition by/of a listed company)
- FEMA (in case of merger of companies having foreign capital)
- Competition Act, 2002- Combination Rules
- Income Tax Act, 1961
- Indian Stamp Act

Applicable Indian Laws

Amalgamations/Mergers

Meaning-Merger/Amalgamation

1. The term 'merger' according to Oxford Advanced Learner's Dictionary(8th edition 2010), means the act of joining two or more organisations into one. Black's Law Dictionary (7thedition) defines 'merger' as the act or an instance of combining or uniting.
2. The term 'amalgamate' according to Oxford Advanced Learner's Dictionary (8th edition 2010), means to put two or more things together so that they form one. If two or more organizations *amalgamate* or *are amalgamated*, they join together to form one large organization. The term 'amalgamate' is synonymous to 'merge'. Black's Law Dictionary (7thedition) gives the meaning of amalgamation as the act of combining or uniting; consolidation – amalgamation of two small companies to form a new corporation.
3. As can be seen from the above definitions, the terms 'merger' and 'amalgamation' are quite synonymous and can be interchangeably used.
4. Generally, the company that merges or amalgamates is known as the 'amalgamating company' or 'transferor company'. The corporate identity of the transferor company ceases to exist post amalgamation. The company into which the amalgamating or transferor company merges or amalgamates is known as the 'amalgamated company' or 'transferee company'.

Types of Mergers

Mergers

- **Horizontal**
  - Between cos. dealing in similar products or competing directly with each other
  - Eg.Vodafone-Idea
- **Vertical**
  - Between cos. operating in the same industry but at a different stage of production or distribution system
  - Eg. eBay and PayPal
- **Conglomerate**
  - Between cos. in unrelated business, no competition
  - Eg ITC Hotels with ITC Ltd
- **Reverse**
  - Between profit and loss making, listed and unlisted
  - Eg. ICICI with ICICI Bank

Mergers- Broad Process

- Valuation & Scheme
- BM for approval of valuation and Scheme;
- Application to NCLT for direction to convene/ dispense with Shareholders & Creditors meeting
- Dispatch of notices and issue of public notice
- Holding of meeting and passing of resolution, if required
- Filing of chairman's report with NCLT, if the meeting has been held
- Filing of second motion application before NCLT- for approval of scheme
- Submission of reports of RD, OL with the NCLT
- Final hearing ,obtaining order, filing order with RoC, post order compliances

The Companies (Compromise, Arrangements and Amalgamations) Rules, 2016

Companies (CAA) Rules, 2016- Procedure (1/5)

- **Rule 3: Form of application**
  - An application for obtaining NCLT Bench's directions to convene a meeting/ dispense with the meeting, shall be in NCLT-1, and shall be supported by an affidavit in NCLT-6 and Notice of admission in NCLT-2.
  - A copy of the proposed scheme of compromise or arrangement is also required to be annexed thereto.
  - Fees- Rs.5000/-

- **Rule 4: Disclosure in the Application**
  - Creditor's responsibility statement in Form No. CAA.1 shall be included in the scheme of corporate debt restructuring.

- **Rule 5: Direction to convene meeting(s)**
  - Upon the hearing the application the Tribunal gives directions in respect of the following matters:-
    - determining the class or classes of creditors and/or of members whose meeting or meetings have to be held; or dispensing with the meeting of class of creditors
    - the time and place of such meeting(s)
    - appointing a chairman for the meeting(s)
    - fixing the quorum and the procedure to be followed at the meeting(s)
    - notice of the meeting and the advertisement of such notice
    - the time within which the chairman of the meeting is to report to the Tribunal the result of the meeting
    - such other matters as the Tribunal may deem necessary.

(Note: Now voting by person or by proxy or by postal ballot or through electronic means is permissible)

Companies (CAA) Rules, 2016- Procedure (2/5)

- **Rule 6: Format for issue of notice calling meeting**
  - The notice of the meeting shall be in Form CAA.2 individually to each class of creditors or members,
  - Notice shall be sent by registered post or speed post or by courier or by e-mail or by any other mode as may be directed by Tribunal atleast one month before the date fixed for the meeting.
  - Notice shall be accompanied by a copy of the proposed Scheme and of the statement required to be furnished under section 230 (3), valuation report, if any and a form of proxy.
- **Rule 7:Advertisement of notice**
- The notice to be advertised in at least one English and one vernacular newspaper having vide circular in the State in which registered office of the company is situated; or in such manner as the Tribunal may direct, not less than 30 days before the date fixed for the meeting in *Form CAA. 2.*

Companies (CAA) Rules, 2016- Procedure (3/5)

- **Rule 8: Notice to statutory authorities**
  - Notice of NCLT convened meeting shall be in form CAA. 3 and shall be accompanied by scheme of compromise or arrangements, explainary statement and disclosure mentioned in rule 6 and shall be sent to-
  - ✓ The Central Government, ROC and IT Authorities, in all cases;
  - ✓ RBI, SEBI, CCI and Stock Exchanges, as may be applicable;
  - ✓ Other sectoral regulators, as may be required by Tribunal
- **Rule 9: Voting**
  - Person entitled to vote may vote in the meeting either in person or through proxy or through postal ballot or through electronic means.
- **Rule 12: Chairman's affidavit for service of notices**
  - The Chairman to file affidavit of service proving dispatch of individual Notices to the shareholders and publication of the Notice in newspapers with respective Court, at least 7 days prior to the date of the meetings.
- **Rule 13: Result of the meeting**
  - The decisions of the meeting(s) held in pursuance of the order made by tribunal on all resolutions shall be ascertained by taking a poll or by voting through electronic means. Report of the meeting shall be in form CAA.4.
- **Rule 14: Submission of chairman's report**
  - The chairman of the meeting(s) shall submission its Report within the time fixed by the tribunal; or where no time has been fixed, within 3 days after the conclusion of the meeting.

Companies (CAA) Rules, 2016- Procedure (4/5)

- **Rule 15: Filing of petition**
  - The Company shall file petition for confirmation of the Scheme in *Form No. CAA.5* within 7 days of filing the Chairman's Report

- **Rule 16: Date and notice of hearing**
  - The tribunal shall fix a date for the hearing of the petition
  - notice of the hearing shall be advertised in the same papers in which the notice of the meeting was advertised, or in such other papers as the tribunal may direct, not less than 10 days before the date fixed for the hearing
  - Notice of hearing shall also be served by tribunal to CG or other authorities who made their representation on scheme.

- **Rule 17: Order on petition**
  - The order sanctioning the Scheme shall include
    - such directions in regard to any matter and such modifications in the compromise or arrangement as the tribunal may think fit to make for the proper working of the compromise or arrangement.
    - The order shall direct that a certified copy of the same shall be filed with the Registrar of Companies within 30 days from the date of the order, or such other time as may be fixed by the tribunal.
    - The order shall be in *Form CAA.6* , with such variations as may be necessary.
- **Rule 20: Issue of Order**
  - An order made under section 232 read with section 230 shall be in *Form CAA.7* with such variation as the circumstances may require

Companies (CAA) Rules, 2016- Procedure (5/5)

- **Rule 21: Statement of compliance in merger and amalgamations**
  - Every Company in relation to which an order u/s 232 (3) is made, shall until the scheme is fully implemented, file with the Registrar, the statement in form CAA.8 alongwith such fees as specified with 210 days from the end of each financial year.

- **Rule 22: Report on working of compromise or arrangement**
  - The tribunal may, at any time after issuing an order sanctioning the scheme, either on its own motion or application made by any interested person, make an order to the company to report on the working of the said compromise or arrangements and on consideration of report, may pass such order as it may deem fit.

- **Rule 23: Liberty to apply**
  - The company or any creditor or member thereof , or in case of company which is being wound up, the liquidator, may , at any time after sanctioning of the scheme by the tribunal, apply to the tribunal for determining questions on working of compromise or arrangements.\

- **Rule 24: Liberty of Tribunal**
  - The tribunal may, at any time during the proceeding, order any petition, information, evidence or statement to be filed in the form of an Affidavit.

Contents of a Scheme

- Appointed Date
  - (w.e.f. MCA's circular dated 21st August, 2019, where the appointed date is ante-dated beyond a year from the date of filing, proper justification must be given)
- Capital Structure
- Objective of Amalgamation
- Vesting of property form the Appointed Date
- Share Exchange Ratio/ Entitlement Ratio
- Accounting Treatment- AS 14/ Ind AS- 103
- Manner of conduct of business of Transferor Company between the Appointed Date and Effective Date
- Effect of amalgamation on contracts/litigations of the Transferor Company
- Service of Employees of Transferor Company
- Dissolution of Transferor Company

Other Aspects of Merger

Whether Holding of Meeting Necessary In all Cases?

- In case of amalgamation of the wholly owned subsidiary companies with their holding company, the court dispensed with the requirement of calling meetings
  - *Punjab Chemicals & Crop Protection Ltd., Re*, (2008) 84 CLA 33 (P&H).
  - *Rajasthan Network (P.) Ltd. v. Synergy Entrepreneur Solutions (P.) Ltd.* [2007] 80 SCL 13 (Raj)

- Where the concerned shareholders gave their written consent to the proposed scheme, their meeting was dispensed with*
  - *NCLAT in DLF Phase- IV Commercial Developers Limited and Others*- Company Appeal (AT) No. 180 of 2019- settled that NCLT has the power to dispense the meeting
    - Dispensation is not mandatory- it is the discretion of NCLT- *NCLAT in* Company Appeal (AT) No.253 of 2018
  - *Celica Developers P. Ltd., Re (No. 1)*, (2005) 145 Com Cases 154 (Cal).
  - *Dabur Foods Ltd, Re*, (2008) 144 Com Cases 378 (Del)
  - *Balaji Industrial Products Ltd., In re* [2008] 88 SCL 321 (Raj.)
  - *Raj Narain Pratap Narain Rolling Enterprises (P.) Ltd.*, In re [2009] 89 SCL 17 (All.)
  - *C.M. Smith & Sons Ltd.,* In re [2009] 89 SCL 377 (Guj.)

**Such consent must be given by atleast 90% of the creditors in value*

Merger of Authorized Capital

- Varied opinion by High Courts as to whether the authorized capital of a transferor company merges into the authorized capital of the transferee company upon the scheme being sanctioned
- Cases decided in negative
  - the Delhi High Court in *Hotline Hol Celdings Pat. Ltd. and Ors* 127 Comp Cas. 165
  - A single bench of Calcutta HC in a scheme presented by *Areva T & D India Limited* (date of judgment- July 7, 2007), decided the issue in negative
- Cases decided in positive
  - In an appeal directed against the said judgment, the division bench of Calcutta High Court **reversed** the above judgment allowing merger of Authorized capital pursuant to the Scheme. *Areva T and D India Limited* [2008] 144 Company Cases 311
  - *Sreeleathers Private Limited & Ors.* (11/11/2008)- Calcutta HC
  - *Surya Commercials Ltd., Re,* (2007) 78 CLA 357 (All);
  - *Om Metals Intraprojects Ltd., Re,* (2007) 80 CLA 143 (Raj)
  - *Ashim Investment Co. Ltd., Re,* (2007) 138 Com Cases 89 (Del).
  - *Ashwin Poultry Farms (India) P.Ltd., Re,* (2007) 138 Com Cases 505 (Mad)
  - *Vasant Investment Corporation Ltd. vs. Official Liquidator, Colaba Land & Mill Co. Ltd. (CP no. 113 of 1979)*

Valuation of Shares

- Principles laid down by the Supreme Court in *Hindustan Lever Employees' Union v. Hindustan Lever Ltd.*, AIR 1995 SC 470
  - Valuation is an art, not an exact science
  - A combination of the yield method, asset value method and market value method was used
  - Courts not to generally question valuation done by independent professional expert and approved by the shareholders

However, recent orders suggest that NCLT is required to supervise the implementation and technical factors such as valuation of shares to determine swap ratio **must** be considered by NCLT.

- ***See*** [*Ankit Mittal v.Ankita Patishthan Ltd. & ors*]

  On an appeal filed against the valuation report of an admitted scheme, the NCLAT held that the Valuation Report was merely based on guess work- hence, the scheme was rejected

- ***In*** [*Wiki Kids Limited*] **,** NCLAT held that-

  "If it shows that there are wide variation in the valuation as can be achieved, it will be desirable that expertise available in the Tribunal has to look so that unfair advantage does not flow to one of the group of shareholders or the other"

With enforcement of the Companies (Registered Valuers and Valuation) Rules, 2017, valuation of shares shall only be done by registered valuers and in strict according to the said Rules

Accounting Standard 14/ Ind-AS 103
Accounting for Amalgamations

Accounting Standard 14 – Accounting for Amalgamations

- **AS 14 recognizes two types of amalgamations:**
  - ***Amalgamation in the nature of merger*** has been defined to mean an amalgamation which satisfies all the following conditions:
    - All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company
    - Shareholders >= 90% of the face value of the equity shares of the transferor company become equity shareholders of the transferee company by virtue of the amalgamation
    - The consideration for the amalgamation is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares
    - The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company
    - No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies
  - ***Amalgamation in the nature of purchase*** is an amalgamation which does not satisfy any one or more of the conditions specified above.

Methods of Accounting

The pooling of interests method- for merger method

- The assets, liabilities and reserves of the transferor company are recorded by the transferee company at their existing carrying amounts (book value)
- Reserves of the transferor company appear in the financial statements of the transferee company in the same form in which they appeared in the financial statements of the transferor company.

The purchase method

- The transferee company accounts for the amalgamation either by incorporating the assets and liabilities at their existing carrying amounts or by allocating the consideration to individual identifiable assets and liabilities of the transferor company on the basis of their fair values at the date of amalgamation
- There is no question of bringing to the books of the transferee the profits/reserves of the transferor
- The amount of the consideration is deducted from the net assets of the transferor company acquired by the transferee company and the difference, if any, is debited to goodwill or credited to Capital Reserve, as the case may be. Goodwill arising on amalgamation is treated as an asset and amortized over a period of five years.

Tax Provisions on Mergers & Amalgamations

Different Cases of Corporate Restructuring and their Tax Issues

Restructuring	Merger/Amalgamation	Sec 2 (1B), Expl 7 to 43 (1), Expl 2 to 43 (6),47 (vi), (vii), 72A , 35DD
	Demerger	2 (19AA), 2(22) (v) 47 (vib), (vic), (vid)
	Takeover of shares	Normal capital gains
	Reduction of capital	2 (22) (d), Income Tax Act
	Buy back of shares	Sec 46A , Sec 115QA
	Slump Sale	Sec 2(42C); 50B
	Others	Conversion of firm into company, company into LLP, etc

Definition of Amalgamation

- As per Section 2(1B) of the Income Tax Act, 1961 "amalgamation", in relation to **companies**, means
  - Merger of one or more companies with another company or
  - Merger of two or more companies to form one company

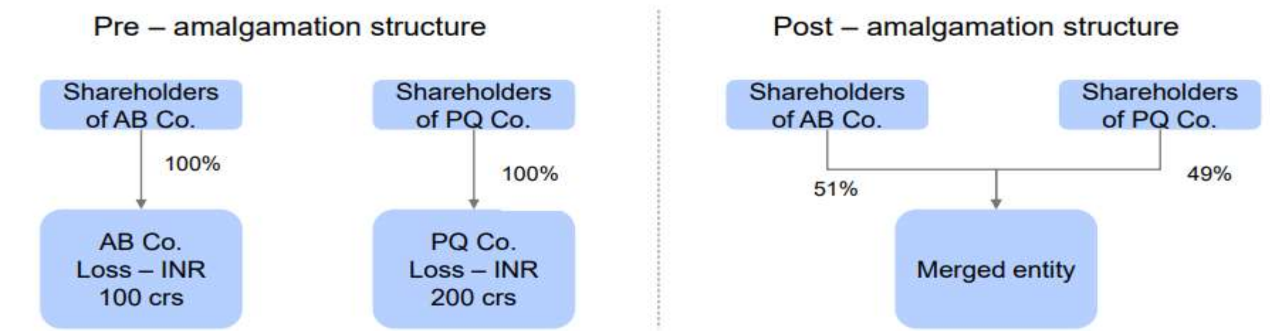
Amalgamation in such a manner that

- **All property of the TRoR is transferred to the TRee**
- **All the liabilities of the TRoR transferred to the TRee**
- **Shareholders >= 3/4th of the TRoR become shareholders of the TRee**

Points to note-

- Merger **as a result of acquisition of property** by one company shall **not** tantamount to merger u/s 2 (1B)
- Merger **as a result of distribution of property** of one company to the other company after the winding up of the first mentioned company shall **not** tantamount to merger u/s 2 (1B)
- W.r.t. the shareholding condition- Shares already held by the TRee co. or its nominees, in the TRoR **shall not be included;**
- The definition is only applicable in case of merger of **companies;**
- So as to avail tax neutrality, the TRee co. (Amalgamated Co.) must be an Indian Company;
- The shares allotted to shareholders of TRoR Co. is **not** subject to any lock-in;
  - A share-swap agreement either pursuant to the Scheme, or otherwise is a common transaction;

Amalgamation –Definition {Section 2(1B)}



Scenario 1	Scenario 2	Scenario 3
AB Co. merges with PQ Co.	PQ Co. merges with AB Co.	AB Co. and PQ Co. merge to form ABPQ Co.
Loss of INR 100 crs available Loss of INR 200 crs to lapse	Both the losses - INR 100 crs & INR 200 crs available for carry forward & set-off	Both the losses - INR 100 crs & INR 200 crs available for carry forward & set-off

Amalgamation-Important aspects

- **Appointed date** is the date from which the scheme becomes effective.
- **Accounting** Accounts of the company would be merged from the appointed date
- ▪**Income tax** : Transferor Company ceases to exist from the appointed date and the Transferee Company would be assessed to tax on the merged income from the appointed date. [**Marshall Sons & Co. (India) Ltd. v. ITO [1997] 233 ITR 809 (SC)]**
- ▪Direct taxes like Advance tax, TDS etc-Appointed date applicable, however practical difficulties
- ▪**Effective date** is the date on which the scheme of merger becomes operative, e.g. the date on which the order of the High Court is filed with the Registrar of Companies

Appointed Date

- General Circular No. 9/2019 dated 21.08.2019 clarified that –
- Section 232(6) enables to choose and state an appointed date in the scheme.
- This date may be a specific calendar date
- Appointed date may be tied to an event such as grant of licence by a competent authority or fulfilment of any preconditions agreed upon by parties.
- Where appointed date chosen is a specific calendar date, it may precede the date of filing the Application, but not beyond a year unless justification brought out in the scheme.

Taxation in Amalgamation- Key Aspects

- Tax Neutrality for company- No capital gain implications [sec 47 (vi)]; depreciation shifts to amalgamated company
- Tax neutrality for shareholders – no transfer on a/c of amalgamation [sec 47 (vii)] holding period is also inclusive
- Carry forward of losses and accumulated depreciation [sec 72A; Rule 9C]
- Amalgamation Expenses and Bad Debts – sec. 35DD
- Apportionment of Depreciation [sec 32(1); 43 (1); 43 (6)]
- Other Aspects
- Important Case Laws

Tax Neutrality in case of Amalgamation (1/2)

Transfer of any capital asset is subject to capital gains tax in India; However, amalgamation enjoys tax-neutrality with respect to tax on transfer.

Tax neutrality u/s 47 for TRoR and TRee

- (vi) TRee is an Indian Co.
- (via) shares in an Indian Co. by a foreign TRoR to a foreign TRee, such that
  - (a) At least 25% of Foreign TRoR become shareholders of foreign TRee
  - (b) such transfer does not attract tax on capital gains in the country, in which the TRoR is incorporated
- (viaa) scheme of amalgamation of a banking co. with a banking inst. Sanctioned by CG
- (viab) amalgamation of a foreign co. (which derives its value substantially from shares of an Indian Co., such that
  - (a) At least 25% of Foreign TRoR become shareholders of foreign TRee
  - (b) such transfer does not attract tax on capital gains in the country, in which the TRoR is incorporated

Tax Neutrality in case of Amalgamation (2/2)

Taxability in the hands of shareholder – Sec 47 (vii) – not regarded as transfer

- any transfer by a shareholder, in a scheme of amalgamation, of a capital asset being a share or shares held by him in the amalgamating company, if—

(a) the transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company except where the shareholder itself is the amalgamated company,

(b) the amalgamated company is an Indian company

Carry Forward of Losses and Unabsorbed Depreciation (1/3)

Conditions to avail carry forward of losses and unabsorbed depreciation

For the Amalgamating Co. (TRoR) Sec 72A (2)(a)

- The TRoR been engaged in the business, **in which the accumulated loss occurred or depreciation remains unabsorbed > 3 yrs**
- **has held continuously as on the date of the amalgamation at least 3/4th of the book value of fixed assets held by it two years prior to the date of amalgamation**

For the Amalgamated Co. (TRee) Sec 72A (2)(b)

- holds continuously for a min. period of 5 yrs from the date of amalgamation at least 3/4th of the book value of fixed assets of the TRoR 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
- fulfils such other conditions as may be prescribed to ensure the revival of the business of the TRoR or to ensure that the amalgamation is for genuine business purpose (see next slide)

Carry Forward of Losses and Unabsorbed Depreciation (2/3)

Conditions for set-off, under Rule 9C [pursuant to sec 72A (2) (b) (iii)]

The TRee (owning an industrial co.) shall:

achieve >= 50% of the installed capacity before the end of 4 years; and maintain till end of 5 years

The TRee shall:

furnish to the Assessing Officer a certificate in Form No.62, duly verified by an accountant, to establish that production levels have been achieved

Carry Forward of Losses and Unabsorbed Depreciation (3/3)

Carry forward of accumulated loss and/or unabsorbed depreciation of the banking company in a Scheme of amalgamation with banking institution (Section 72AA)

- In a Scheme of amalgamation of a banking company with a banking institution sanctioned and brought into force by the Central Government u/s. 45(7) of the Banking Regulation Act, 1949, the accumulated loss and unabsorbed depreciation of the banking company can be carried forward by the the banking institution for set off against its profits.

Carry Forward of Losses and Unabsorbed Depreciation

Points to note-

- **All** conditions (u/s 72A (2)(a) and (b)) must be fulfilled.
- W here such conditions are fulfilled,
  - Accumulated loss of the TRoR will be allowed to carried forward for a <u>**fresh period** of 8 years;</u>
    - *Supreme Industries Ltd. vs DCIT :2007 17 SOT 476 (Mum ITAT)*
  - <u>Unabsorbed depreciation</u> can be carried forward <u>**indefinitely**</u>

- If the conditions mentioned in the previous slide are **not** fulfilled- [Sec. 72A (3)]
  - The set off of loss or allowance of depreciation made in any previous year in the hands of the TRee Co.
  - Shall be deemed to be the income of the TRee Co. chargeable to tax
  - For the year in which such conditions are not complied with.
- **Accumulated loss** means loss of the TRoR under the head "Profit and Gains of business or profession" **(not being a loss due to speculation business)**
- **Accumulated losses b/f under the head "house property" or "capital gain" will get lost, and neither co. will be able to avail c/f benefit**

Apportionment of Depreciation

For apportionment of depreciation b/w the TRoR and TRee, following steps should be followed [proviso to S. 32(5)]

- Assume that there has been no amalgamation; and compute depreciation for the TRoR;
- Once computed, the depreciation amount shall be:
  - Apportioned b/w the TRoR and TRee
  - In the ratio of the number of days for which the assets were used by them

Apportionment of depreciation

- Co A engaged in manufacturing of Tea
- As per the Income-tax provisions, only 40% of the profits are liable to tax
- Co A mergers into Co B
- Appointed date – April 1, 2014
- What will be the WDV of Fixed assets of Co A in the hands of Co B????

WDV in books of Co A

A.Y.	Gross Block	Depreciation	Net Block
2012-13	2000	300	1700
2013-14	1700	250	1450
2014-15	1450	210	1240

1696 = 2000 – (300+250+210)*40%

CIT vs Doom Dooma India Ltd. [2009] 178 Taxman 261:

Words 'depreciation actually allowed' would mean depreciation deducted in arriving at the taxable income or the depreciation deducted in arriving at the income (composite income); since in cases where Rule 8 applies income which is brought to tax 'business income' is only 40% of the composite income, only 40% depreciation allowed at prescribed rate is required to be taken into account because that is depreciation 'actually allowed'

Amalgamation Expenses and Bad Debts

Amortisation of amalgamation expenses [sec. 35DD]

- Where an **Indian Co.;**
- Incurs any expenditure **wholly or exclusively for the purpose of amalgamation;**
- Deduction = 1/5th of such expenditure
    - For each of the 5 successive years
    - Beginning in the prev. year in which amalgamation was done
- Shall be given to the TRee

Treatment of Bad-debts [sec. 36 (1) (vii)

- Where the debts of the TRoR, transferred to the TRee becomes bad;
- Such bad debts will be allowed as a deduction to the TRee

[CIT v.T.Veerabhadra Rao, K. Koteswara Roa & Co. (1985) 155 ITR 152 (SC)]

Other Aspects

- As per **Section 2(42A)** of the Act, Period of Holding of the shareholders for the amalgamated company shall include period for which the shares were held in the amalgamating company.
- As per **section 49(1)** of the Act, the cost of acquisition of the said asset to the amalgamated company shall be cost for which the amalgamating company acquired it
- As per **Section 49(2)** of the Act, the cost of acquisition of the shares for the shareholders in the amalgamated company shall be the cost of acquisition of the shares in the amalgamating company.

- If capital asset was acquired by the amalgamating company before 01.04.2001 then COA may be taken as the cost or F.M.V. as on 01.04.2001, whichever is higher – sec 55 (2)
- The cost of improvement incurred by the amalgamating company shall be deemed to be the cost of improvement incurred by the amalgamated company.
- **Explanation 13 to Sec. 43 (1)-** Actual Cost of Asset on which deduction is allowed
  - When the actual cost of the asset has been allowed as
    - deduction U/s 35D to the amalgamating company
  - The actual cost of the asset to the amalgamated company shall be NIL

Important Case Laws (1/3)

- Tax Neutrality [Section 47(vii)] will not be applicable where
  - the shareholder of the amalgamating company
  - is allotted bonds or debentures in exchange of shares in the amalgamating company –

  [CIT vs. Gautam Sarabhai Trust : 173 ITR 216 (Guj.)]

- On amalgamation, rights of shareholder of the TRoR in the capital asset, i.e., the shares stand extinguished, resulting in a transfer under section 2(47)

  [CIT vs. Mrs. Grace Collis and Ors. :248 ITR 323 (SC)]

Important Case Laws (2/3)

ITA does not explicitly deal with the issue of whether depreciation under s. 32 is available on goodwill

- The Supreme Court in the case of **Smifs Securities Ltd. (2014) (24 taxmann.com 222) (SC)** held as follows:
- Goodwill is a depreciable asset under s. 32(1)(ii).
- The difference between the cost of an asset (net assets) and the amount paid constitutes goodwill.
- The amalgamated company, in the process of amalgamation, had acquired a capital right in the form of goodwill because of which its market worth stood increased
- The above view has been recently affirmed by ITAT Mumbai in the case of **DCIT vs Toyo Engineering India Limited (ITA No 3279/M/2008)** wherein it held that depreciation should be allowed on Goodwill arising on amalgamation

Important Case Laws (3/3)

- Whether, TRee would be entitled to carry forward and set off of credit of Minimum Alternate Tax available to the TRoR under section 115JAA of the Income Tax Act.?

YES. *[Refer: SKOL Breweries Ltd. v. ACIT, 28 ITAT India 998 (Mum.) ITA No. 313/Mum./07 A.Y. 2003-04 dated 15-5-2008]*

M/s. Caplin Point Laboratories Ltd. v. Assistant Commissioner of Income-tax Order dated January 31, 2014 in ITA No.667/Mds/2013 (ITAT Chennai).]

Ambuja Cements Ltd. v. Deputy Commission of Income-tax Order dated September 5, 2019 in ITA no.3643/Mum./2018 (ITAT Mumbai).

Thank you!!

Any Questions?

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