

Direct Tax Code Bill, 2009

Business Reorganisation / GAAR

Bombay Chartered Accountant Society

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Business Reorganisation

Business Reorganisation

Parameters	Existing	Proposed in DTC
Definition	▶ No definition	▶ Reorganisation of business of two or more residents, involving: <ul style="list-style-type: none">▶ Amalgamation▶ Merger under a scheme sanctioned by Central Government under Banking Regulation Act or▶ Demerger
Scope	▶ N.A	▶ Restricted to reorganisation between residents only

Amalgamation: Definition

Parameters	Existing	Proposed in DTC
For companies	<ul style="list-style-type: none"> ▶ All assets and liabilities are transferred ▶ Shareholders holding 3/4th in value become shareholders of amalgamated company 	<ul style="list-style-type: none"> ▶ Same ▶ Same ▶ Amalgamation to be in accordance with Companies Act, 1956
For unincorporated body	<ul style="list-style-type: none"> ▶ All assets and liabilities are transferred ▶ Partners / proprietor become shareholder in proportion of their capital account ▶ No consideration other than shares ▶ Shareholding of all the Partners / Proprietor in the Company is at least 50% of the total voting power and such holding continues for 5 years. 	<ul style="list-style-type: none"> ▶ Same ▶ Same ▶ Same ▶ No time limit for holding prescribed, only allotment of at least 50% of value of shares required

Amalgamation: Eligibility

Parameters	Existing	Proposed in DTC
For companies	<ul style="list-style-type: none">▶ Merger of company(ies) [including foreign company(ies)] with an Indian company	<ul style="list-style-type: none">▶ Merger of Two or more 'Resident' Companies
For unincorporated body	<ul style="list-style-type: none">▶ Succession of Firm / Proprietary Concern into a Company	<ul style="list-style-type: none">▶ Covered as Amalgamation and scope extended to AOP / BOI also▶ Covers amalgamation with 'Amalgamated' Company

Amalgamation: Key Aspects

Parameters	Existing	Proposed in DTC
Neutrality of capital gains - Amalgamating Company and Shareholder	<ul style="list-style-type: none"> ▶ Tax neutral ▶ Exemption to all Capital Asset 	<ul style="list-style-type: none"> ▶ Tax neutral ▶ Exemption to Investment Asset <ul style="list-style-type: none"> ▶ Is Business Capital Asset covered? ▶ Unincorporated Body Succession – would it be covered under Slump Sale definition?
Cost of acquisition of investment Assets	<ul style="list-style-type: none"> ▶ Continues to be the same cost as in the hands of the amalgamating company 	<ul style="list-style-type: none"> ▶ Same
Cost of Acquisition of Business Capital Asset	<ul style="list-style-type: none"> ▶ No such distinction – part of Capital Asset only 	<ul style="list-style-type: none"> ▶ No Specific provision for such assets which are not depreciable
Continuity of Depreciation / WDV for business capital assets	<ul style="list-style-type: none"> ▶ If amalgamation during the year - proportionate depreciation ▶ WDV in the hands of amalgamating company to continue in the hands of the amalgamated company 	<ul style="list-style-type: none"> ▶ Same ▶ Same

Amalgamation: Other provisions

Parameters	Existing	Proposed in DTC
Continuity of period of holding of asset	<ul style="list-style-type: none"> ▶ Period of holding of capital asset in hands of Amalgamating Company made part of period of holding of Amalgamated Company 	<ul style="list-style-type: none"> ▶ No specific provision for continuity of period of holding of investment asset
Reorganisation (including Amalgamation) Expenditure	<ul style="list-style-type: none"> ▶ No distinction of Revenue Expenditure and Deferred Revenue Expenditure ▶ Allowance @ 1/5th over five years 	<ul style="list-style-type: none"> ▶ Revenue Expense allowed in the year of expenditure. Depreciation @ 25% on Deferred Revenue Expenditure
Transfer of asset in Indian company by predecessor foreign company to successor foreign company	<ul style="list-style-type: none"> ▶ Applicable to shares in Indian Company ▶ Exempt only if atleast 25% of the shareholders continue to remain shareholders ▶ Tax neutral in foreign country 	<ul style="list-style-type: none"> ▶ Applicable to all investment assets ▶ No such condition ▶ Same

Amalgamation: Carry forward of losses

Parameters	Existing	Proposed in DTC
Eligibility for Losses of Amalgamating company	<ul style="list-style-type: none"> ▶ Specified banking company/ Hotels/ ships/ industrial undertaking owning company ▶ Business loss and unabsorbed depreciation 	<ul style="list-style-type: none"> ▶ All companies are eligible ▶ Business loss, unabsorbed depreciation and capital loss
Pre-Business conduct conditions	<ul style="list-style-type: none"> ▶ Business (where loss incurred) continued for 3 years ▶ 75% fixed asset base continuous holding for 2 years prior to amalgamation date 	<ul style="list-style-type: none"> ▶ No pre business conduct conditions
Business Continuity Conditions	<ul style="list-style-type: none"> ▶ The Amalgamated Company holds at least 3/4th of the book value of fixed assets acquired for 5 years ▶ Amalgamated Company continues the business of the Amalgamating Company for 5 years ▶ Compliance with other conditions as may be prescribed (i.e. 50% of capacity utilisation level before end of 4th year) 	<ul style="list-style-type: none"> ▶ Same ▶ Same ▶ Compliance conditions to be prescribed

Amalgamation: Carry forward of losses

Parameters	Existing	Proposed in DTC
Continuity in case of Unincorporated Body	▶ Shareholding of the Partners / Proprietor continue to be > 50% for 5 years	▶ Same
If above conditions not fulfilled	▶ Loss deemed to be wrongly allowed to be rectified	▶ Same

Demerger: Definition

Parameters	Existing	Proposed in DTC
Definition	<ul style="list-style-type: none"> ▶ All assets and liabilities are transferred ▶ Assets and liabilities are transferred at 'Book' Value ▶ Resulting Company issues shares to the shareholders of Demerged Company on proportionate basis ▶ Shareholders holding 3/4th in value become shareholders of the resulting company ▶ Transfer on a going concern basis ▶ Other prescribed conditions 	<ul style="list-style-type: none"> ▶ Same ▶ Same ▶ Resulting Company issues 'Equity' shares to the shareholders of Demerged Company on proportionate basis ▶ Same ▶ Same ▶ Conditions to be prescribed
Allocation of General Liabilities	<ul style="list-style-type: none"> ▶ Specific Provision 	<ul style="list-style-type: none"> ▶ No Specific Provision

Demerger: Key Aspects

Parameters	Existing	Proposed in DTC
Eligibility	<ul style="list-style-type: none"> ▶ Foreign company's demerging into Indian Company covered 	<ul style="list-style-type: none"> ▶ Demerger between 'residents' only
Neutrality of capital gains - Demerged / Resulting Companies and Shareholder	<ul style="list-style-type: none"> ▶ Tax neutral 	<ul style="list-style-type: none"> ▶ Tax neutral ▶ No specific provision for exemption in hands of shareholders ▶ Exemption in relation to Investment Asset only <ul style="list-style-type: none"> ▶ Is Business Capital Asset covered?
Cost of Acquisition of assets	<ul style="list-style-type: none"> ▶ No Specific Provision – considered at 'book' value being the value at which transferred 	<ul style="list-style-type: none"> ▶ Cost of investment asset as in the hands of the Demerged Company becomes cost to the Resulting Company
Cost of Acquisition of non-depreciable Business Capital Asset	<ul style="list-style-type: none"> ▶ No such distinction – part of Capital Asset only 	<ul style="list-style-type: none"> ▶ No Specific provision for such assets which are not depreciable

Demerger: Key Aspects

Parameters	Existing	Proposed in DTC
Continuity of depreciation / WDV for Business Capital Assets	<ul style="list-style-type: none"> ▶ If demerger during the year - proportionate depreciation ▶ WDV in the hands of predecessor to continue in the hands of the successor ▶ Block of Asset of Demerged Company to be reduced to the extent of WDV transferred 	<ul style="list-style-type: none"> ▶ Same ▶ Same ▶ No specific provision relating to reduction of WDV in hands of predecessor
Continuity of period of holding of asset	<ul style="list-style-type: none"> ▶ Period of holding of capital asset in hands of Demerged Company included in period of holding of Resulting Company 	<ul style="list-style-type: none"> ▶ No specific provision for continuity of period of holding of investment asset
Reorganisation (including Demerger) Expenditure	<ul style="list-style-type: none"> ▶ No distinction of Revenue Expenditure and Deferred Revenue Expenditure ▶ Allowance @ 1/5th over five years 	<ul style="list-style-type: none"> ▶ Revenue Expense allowed in the year of expenditure. Depreciation @ 25% on Deferred Revenue Expenditure
Transfer of asset in Indian company by predecessor foreign company to successor foreign company	<ul style="list-style-type: none"> ▶ Applicable to shares in Indian Company ▶ Exempt only if shareholders holding at least 3/4th in value continue to remain shareholders ▶ Tax neutral in foreign country 	<ul style="list-style-type: none"> ▶ Applicable to all investment assets ▶ No such condition ▶ Same

Demerger: Carry forward of losses

Parameters	Existing	Proposed in DTC
Eligibility for Losses of Demerged company	<ul style="list-style-type: none"> ▶ All Resulting company were entitled ▶ Directly relatable to business activity transferred, else proportionate loss 	<ul style="list-style-type: none"> ▶ Same ▶ Specific provision allows transfer of losses of Demerged Company.
Business Continuity Conditions	<ul style="list-style-type: none"> ▶ No such Condition ▶ No such Condition ▶ No such conditions 	<ul style="list-style-type: none"> ▶ The successor holds at least 3/4th of the book value of fixed assets acquired for a period of 5 years ▶ Continues the business of the predecessor for a period of 5 years ▶ Compliance with conditions as may be prescribed
If above conditions not fulfilled	<ul style="list-style-type: none"> ▶ N.A. 	<ul style="list-style-type: none"> ▶ Loss deemed to be wrongly allowed to be rectified.

Slump Sale

Slump Sale

Parameters	Existing	Proposed in DTC
Taxability	<ul style="list-style-type: none"> ▶ Taxable as capital gains 	<ul style="list-style-type: none"> ▶ Taxable as business income
Cost of acquisition - seller	<ul style="list-style-type: none"> ▶ Cost of acquisition to be net-worth ▶ Basis of net-worth computation laid out 	<ul style="list-style-type: none"> ▶ Same ▶ Basis of net-worth computation to be prescribed
Cost of acquisition – acquirer	<ul style="list-style-type: none"> ▶ Allocation of purchase price 	<ul style="list-style-type: none"> ▶ Uncertain - cost to previous owner or actual purchase price for business capital asset? ▶ Slump sale may include investment assets also – cost thereof ?
TDS in case of resident	<ul style="list-style-type: none"> ▶ N.A. 	<ul style="list-style-type: none"> ▶ 10% on entire sales consideration ▶ In case of default at the time of acquisition or on expenditure on sale, cost/ expenses may not be deductible on future sale

Acquisition of shares

Parameters	Existing	Proposed in DTC
Capital Gains	<ul style="list-style-type: none"> ▶ Long term and short term capital gains distinguished ▶ Taxable at different rates 	<ul style="list-style-type: none"> ▶ Distinction of long term and short term gain removed ▶ Taxable @ 25% in case of companies <ul style="list-style-type: none"> ▶ Taxable @ 30% in case of foreign companies in some cases
TDS in case of Resident	<ul style="list-style-type: none"> ▶ N.A. 	<ul style="list-style-type: none"> ▶ 10% on entire sales consideration ▶ In case of default at the time of acquisition or on expenditure on sale, cost / expenses may not be deductible
Income deemed to accrue in India	<ul style="list-style-type: none"> ▶ Indirect Transfer of Capital Asset was not specifically covered 	<ul style="list-style-type: none"> ▶ Indirect transfer of Capital Asset specifically covered
Scope of closely held companies narrowed	<ul style="list-style-type: none"> ▶ Listed Companies / subsidiaries of listed companies and other specified Corporations are not closely held companies 	<ul style="list-style-type: none"> ▶ Public companies are not closely held companies. ▶ Private companies wherein >50% is held by Public companies are also not covered ▶ A private company which is subsidiary of a Foreign Company satisfying conditions defining a public company also will not be covered.
Losses of closely held companies	<ul style="list-style-type: none"> ▶ Ownership change – Business & capital losses lapses ▶ Unabsorbed depreciation not impacted 	<ul style="list-style-type: none"> ▶ Ownership change – Business losses and unabsorbed depreciation lapses ▶ Capital losses not impacted

Other Provisions

Parameters	Existing	Proposed in DTC
Non-Compete fees	▶ Considered as revenue expenditure	▶ Depreciation @ 25%
Cost of Acquisition	▶ Not specifically defined	▶ Defined to be Purchase price, which is not further defined ▶ Whether incidental cost, finance cost etc. will be allowed ? ▶ What will be cost in case of non cash transfers?
Cost identification in case of dematerialised share	▶ FIFO basis	▶ No specific provision
Deferred Consideration – taxability	▶ Not specified	▶ Not covered
Amortisation of goodwill	▶ Not explicitly covered	▶ Not covered
Conversion of partnership firm / company into LLP	▶ Not covered	▶ Not covered

General Anti-Avoidance Rule ('GAAR')

General Anti-Avoidance Rule...

- Empowers the Commissioner of Income-tax ('CIT') to declare an arrangement impermissible
 - if the arrangement has been entered with the objective of obtaining tax benefit **and**, inter alia, lacks commercial substance or misuses the provisions of the Code
- CIT may amend, disregard or re-characterise the arrangement
- Onus on the tax payer to demonstrate obtaining tax benefit was not the main purpose of the arrangement
- Applicable to residents as well as non-residents

...General Anti-Avoidance Rule

- GAAR provisions are highly subjective
- Sweeping powers to tax department
- Whether tax planning permissible ?
- Specific provisions should be introduced to control tax evasions
 - Specific anti avoidance rules prevailing in other jurisdictions --Treaty shopping, Base companies, Thin capitalization, Round tripping, CFC, etc.

Thank You

