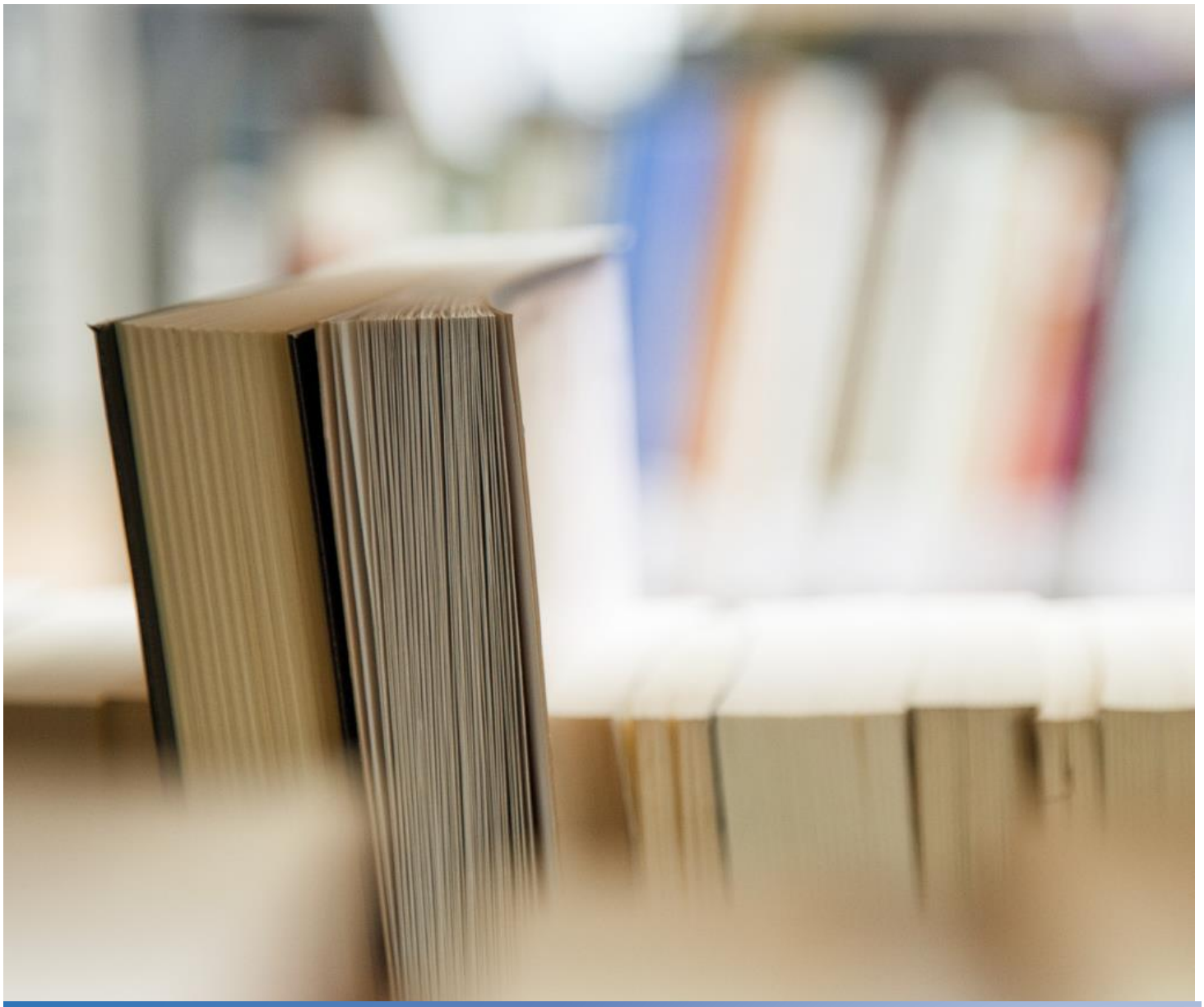

# MERGERS AND ACQUISITIONS – GST PERSPECTIVE

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# Mergers and Acquisitions – GST Perspective

## Introduction

In today's era, business combinations are very frequent and can create different types of synergies based on the objective of such combinations.

In case of a merger, there is a legal process through which two or more companies join together to form a new entity or wherein one company is completely absorbed by the other through which the amalgamating company loses its existence. In case of acquisition, one company sells the complete company or an undertaking to the other company. Demerger is another type of arrangement wherein part or whole of the undertaking of one company is hived off to another company which operates completely separate from the original company.

These business combinations require a due diligence and in-depth cost benefit analysis. This cost benefit analysis requires an understanding of the impact of GST on such transactions.

## Deemed supply and its exception

As per clause 4(c) of the Schedule II of the CGST Act 2017:

*"where any person ceases to be a taxable person, any goods forming part of the assets of any business carried on by him shall be deemed to be supplied by him in the course or furtherance of his business immediately before he ceases to be a taxable person, unless—*

*(i) the business is transferred as a going concern to another person; or*

*(ii) the business is carried on by a personal representative who is deemed to be a taxable person."*

As per the above, if the transferor ceases to be registered and liable to be registered under the GST law due to any business combination, the goods forming part of the

assets of the business within it is deemed to be supplied. However, where such business is transferred as a going concern, then it will not be considered as a deemed supply.

**Going concern test**

The most important test that is applied here is whether such supply amounts to transfer of the undertaking as a whole on going concern basis.

GST law does not specifically cover the meaning of the term 'undertaking' or 'slump sale'. So, one may need to refer to the definition of 'slump sale' as given under Section 2(42C) of the Income Tax Act, 1961. As per the said definition:

*"Slump sale means the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales.*

*Explanation 1 – For the purposes of this clause, "undertaking" shall have the same meaning assigned to it in Explanation 1 to clause (19AA)"*

As per Explanation 1 to clause (19AA) of the Income Tax Act, 1961:

*"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 include individual assets or liabilities or any combination thereof not constituting a business activity"*

From the above, it can be inferred that there should be an ongoing business activity for the transferor in order to be called as an undertaking and to fall within the ambit of slump sale.

Also, in order to strengthen our argument, we can refer to the following judgements:

In *Equinox Solution Pvt Ltd* [TS-149-SC-2017], the Supreme Court held that where the entire business is sold off as a going / running concern, then it would be considered as a slump sale.

Further, in the case of *Commissioner of Income Tax vs Max India Ltd* [2009] 319 ITR 68(P& H), it has been held that if the business can be carried on without any interruption based on the transferred assets and liabilities of a business, then it would amount to slump sale.

As per the above judicial precedents, it can be interpreted that the transfer should be as a going concern for it to be a slump sale and the unit should be able to function independently and continuously without any interruption. However, if only some assets are combined and sold in a consolidated manner without the assurance that the same will result in the business running without interruption, the same would not fall within going concern.

**Supply of goods or services?**

Also, the GST law does not expressly provide what constitutes a slump sale. However, referring to the judgements in the VAT law, it was held in the case of *Paradise Food vs State of Telangana* [2017] 81 taxmann.com 331 (Andhra Pradesh) that the transfer of business as a whole could not be considered as sale of goods.

As per Section 2(102) of the CGST Act, 2017 services have been defined as:

*"Services means anything other than goods, money and securities but includes activities relating to the use of money or its conversion by cash or by another mode, from one form, currency or denomination to another from, currency or denomination for which a separate consideration is charged".*

With the wide nature of definition of service given above and the fact that services tend to include anything other than goods, transfer of undertaking can at best amount to a supply of service.

**Exempt or Taxable supply?**

To get an indication of the nature of services which the GST law purports to cover, one should carefully look at the list of services on which various tax rates and exemptions have been provided. Out of the list given, only one particular item covers the transfer

of undertaking as per the exemption notification No. 12/2017-Central Tax (rate) dated 28th June, 2017. This exemption reads as under:

*"Services by way of transfer of a going concern, as a whole or an independent part thereof"*

Only if the assets and liabilities are transferred in such a way that the business can be carried on as such on-going concern basis, such transfer will be treated as exempt supply of services. It has already been discussed above as to what will constitute going concern. Unless the assets and liabilities transferred are such that they allow a business to be carried on as such without any interruption, it will not be considered as a going concern.

Where some assets are supplied together which are not capable of running a business on its own, the transfer without going concern will be treated as a taxable supply. In such a situation, the assets which are transferred will be treated a mixed supply. In case of a mixed supply, two or more individual supplies are supplied together which are not naturally bundled. The rate of tax in case of such supplies is to be taken as the highest of the rate applicable on each of the individual supplies.

**Input tax credit**

It has already been discussed above that where the assets of a business are transferred due to any business combination which is not on a going concern basis, the said transfer will constitute a mixed taxable supply. In such cases, the input tax credit can freely be taken against such outward taxable supplies for the transferor. Further, the tax paid on such transfer by the transferee will also be eligible as input tax credit to such person.

Wherein the transfer is on a going concern basis, it is already discussed above that the said transfer will be considered as exempt. However, there is a provision for transfer of input tax credit held by the transferor to the transferee subject to certain conditions. As per Section 18(3) of the CGST Act 2017:

*"Where there is a change in the constitution of a registered person on account of sale, merger, demerger, amalgamation, lease or transfer of the business with the specific provisions for transfer of liabilities, the said registered person shall be allowed to transfer the input tax credit which remains unutilised in his electronic credit ledger to such sold, merged, demerged, amalgamated, leased or transferred business in such manner as may be prescribed."*

This means that only if there is a specific provision for transfer of liabilities, the registered person will be allowed to transfer the input tax credit unutilized in his electronic credit ledger. Without the transfer of liabilities, the input tax credit cannot be transferred either. In case of demerger, the input tax credit is to be apportioned in the ratio of the value of the assets of the new units as per the demerger scheme.

The steps for the transfer of input tax credit in case of various business combinations (like sale, merger, demerger, amalgamation, lease or transfer) can be derived from Rule 41 of the CGST Rules 2017:

a) Transferor will furnish Form GST ITC-02 along with a request for transfer of unutilized input tax credit lying in his electronic credit ledger to the transferee

b) The transferor will also submit a copy of a certificate issued by a Practicing Chartered Accountant or Cost Accountant certifying that the sale, merger, de-merger, amalgamation, lease or transfer of business has been done with a specific provision for the transfer of liabilities

c) The transferee shall, on the common portal, accept the details so furnished by the transferor and, upon such acceptance, the un-utilized credit specified in FORM GST ITC-02 shall be credited to his electronic credit ledger

d) The inputs and capital goods so transferred shall be duly accounted for by the transferee in his books of account.

## Conclusion

Thereby, from the above, it can be interpreted that in case of any business combination, the primary aspect to determine is whether there is a provision for transfer of liabilities and whether the said transfer is on going concern basis. If the answer is in the affirmative, then the supply will be exempt and the ITC can be transferred from the transferor to the transferee. If the answer is negative, then it will constitute a taxable mixed supply and the Input tax credit can be taken by both the transferor and transferee for their respective inward supplies.


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