

Income Tax Implication on Specified Transactions

Lesson 3

KEY CONCEPTS

■ Dividend Income ■ Buy Back of Shares ■ Slump Sale ■ Transfer of Shares ■ Reduction of Share Capital ■ Equalization Levy ■ Carbon Credit ■ Amalgamation

Learning Objectives

To understand the:

- Tax implication on Dividend Income
- What is buy back of shares and the tax implication in case of buy back of shares
- What is slump sale and tax implication in case of slump sale?
- Tax implication in case of transfer of shares
- The tax implication on Reduction of Share Capital
- The Concept of Equalization Levy
- The Concept of Carbon Credit
- Tax Implication in case of Restructuring of Business (Amalgamation / Merger / Demerger)

Lesson Outline

- Introduction
- Taxation on Dividend Income
- Buy Back of Shares
- Tax Implication on Buy Back of Shares
- Slump Sale
- Tax Implication on Slump Sale
- Tax implication on Transfer of Shares
- Tax implication on Reduction of Share Capital
- Equalization Levy
- Carbon Credit
- Amalgamation / Merger
- Demerger
- Questions for Practice
- Lesson Round Up
- Test Yourself
- List of Further Readings
- Other References

REGULATORY FRAMEWORK

| Sections (Income Tax Act, 1961) | Details |
|--|--|
| Section 2(22)(a) to (f) | Dividend Income |
| Section 57(i) | Deduction of interest expenses for earning a dividend income |
| Section 80M | Deduction in respect of certain Inter Corporate Dividend |
| Section 10(34B) | Exemption for inter-corporate dividend distribution within IFSC Units engaged in the aircraft leasing business |
| Section 2(42C) | Slump Sale |
| Section 50B | Special provision for computation of capital gains in case of slump Sale |
| Section 50CA | Special provision for full value of consideration for transfer of share other than quoted share |
| Section 115BBG | Carbon Credit |
| Section 165/165A | Equalization Levy |
| Section 2(1B) | Amalgamation |
| Section 2 (19AA) | Demerger |
| Section 72A | Carry Forward and Set Off of Accumulated loss and unabsorbed depreciation of the amalgamating company |

TAXATION OF DIVIDEND INCOME**Dividend Income**

For the purposes of inclusion in the total income of an assessee-

- (a) any dividend declared by a company or distributed or paid by it within the meaning of sub-clause (a) or sub-clause (b) or sub-clause (c) or sub-clause (d) or sub-clause (e) or sub-clause (f) of clause (22) of Section 2 shall be deemed to be the income of the previous year in which it is so declared, distributed or paid, as the case may be;
- (b) any interim dividend shall be deemed to be the income of the previous year in which the amount of such dividend is unconditionally made available by the company to the member who is entitled to it.

Dividend can be categorized into two categories Actual Dividend and Deemed Dividend u/s 2(22)(a) to (f).

Dividend is taxable in hands of Shareholders at Normal Rates and Exempt in the hands of Company.

Taxability in hands of Shareholders

In hands of Resident Shareholder, the Dividend so received is Taxable at Normal Rates (Default Regime or Optional Regime) whereas in hands of Non-Resident Shareholder the Dividend received is taxable at Special Rates as per Section 115A and deduction of interest u/s 57(i) is allowed up to a maximum of 20% of such dividend income

Taxability of Dividend in the hands of Company

Dividend so declared is Exempt in hands of Company. Earlier DDT/CDT u/s 115-O was applicable, No Deduction u/s 57 allowed.

| Nature of Dividend | Taxability (at Normal Rates) |
|--------------------|--|
| Final | In the year of declaration at the AGM by Company |
| Deemed | In the year of distribution paid by the Company |
| Interim | In the year of receipt by the shareholders |

Section 2(22): Dividend Includes:

| Distribution by a Company to Shareholders | | | | Loan or Advance by Company not covered u/s 2(18) | Buyback of Shares | |
|--|--|---|---|--|--|--|
| Section 2(22)(a) | Section 2(22)(b) | | Section 2(22)(c) | Section 2(22)(d) | Section 2(22)(e) | Section 2(22)(f) |
| Any of the Assets (100% or Part of the Assets) | Debentures, debenture-stock, deposit certificate with or without interest. | Bonus shares to preference shareholders | Any money or asset on its liquidation to Equity Shareholder | Any money or asset on Reduction of its capital to Equity Shareholder | To Shareholder (min 10% equity holding) or concern in which such shareholder has substantial interest or to any person for benefit of such shareholder | any payment by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 68 of the Companies Act, 2013 |

but "dividend" does not include—

- (i) a distribution made in accordance with sub-clause (c) or sub-clause (d) in respect of any share issued for full cash consideration, where the holder of the share is not entitled in the event of liquidation to participate in the surplus assets;
- (ia) a distribution made in accordance with sub-clause (c) or sub-clause (d) in so far as such distribution is

attributable to the capitalised profits of the company representing bonus shares allotted to its equity shareholders after the 31st day of March, 1964, and before the 1st day of April, 1965 ;

- (ii) any advance or loan made to a shareholder or the said concern by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company ;
- (iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off;
- (v) any distribution of shares pursuant to a demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).

Tax Implication in case of Dividend Income

Upto 31.03.2020

Dividend Received by shareholders from Domestic Company were exempt u/s 10(34) and Domestic Companies declaring (distributing) dividend were liable to Corporate Dividend Tax (CDT) / Dividend Distribution Tax (DDT) u/s 115-O. Finance Act, 2020 abolished the DDT (Dividend Distribution Tax) and moved to classical system of taxation where dividend is taxed in hands of shareholders.

From 01.04.2020

Dividend received by shareholders from Domestic Companies is taxable in hands of shareholders only and DDT was abolished.

| | |
|-------------------------|--|
| Domestic Company | All Indian Co's and other (Foreign) Co's who have made prescribed arrangements for declaration & distribution of Dividend in India |
| Indian Company | Any Company formed & Registered by Companies Act, 2013 or earlier Acts |
| Foreign Company | A Company which is not a Domestic Company |

Dividend Distribution Tax 'DDT' [Section 115-O]: It was a tax on dividend (interim or final) declared, distributed or paid by a company (whether out of current or accumulated profits). Dividend distribution tax is in addition to income tax on total income. However, **the provisions of section 115-O (1) shall not be applicable w.e.f. April 1, 2020 as dividend shall now taxable in the hands of the recipient [As amended by Finance Act, 2020].**

The Finance Act, 2020 has abolished the DDT and move to the classical system of taxation wherein dividends are taxed in the hands of the investors. Therefore, the provision of Section 115-O shall not be applicable if the dividend is distributed on or after 01-04-2020. **Thus, if the dividend is distributed on or after 01-04-2020 the domestic companies shall not liable to pay DDT and, consequently, shareholders shall be liable to pay tax on such dividend income.** As dividend would now be taxable in the hands of the shareholder, various provisions of the Act have been revived such as allowability of expenses from dividend income, deductibility of tax from dividend income, treatment of inter-corporate dividend, etc.

As per the Finance Act, 2020 amended Section 57(i), effective from April 1, 2021 states that a taxpayer can claim a deduction of interest expenses for earning a dividend income (other than any payment by a company on purchase of its own shares from a shareholder i.e. buy-back of shares) and Interest on money borrowed for investing in the shares can be claimed as a deduction **subject to a maximum of 20% of dividends or income** in respect of units of a mutual fund **i.e.**

- a) **Actual expenses or**
- b) **20% of Dividend or Income**

whichever is lower.

In nut shell, taxpayer cannot claim a deduction of any expense against dividend income, except interest expense on cash borrowed for investment (in Shares, UTI or MF) and the dividend income will be taxable. It is immaterial of the sum received at applicable income tax slab rates.

Inter-corporate Dividend relief: As the taxability of dividend has been shifted from companies to shareholders w.e.f. 01.04.2020, the Government has introduced **a new section 80M** under the Act to remove the cascading effect where a domestic company receives a dividend from another domestic company. However, nothing has been prescribed where a domestic company receives dividend from a foreign company and further distribute the same to its shareholders. **[As Amended by Finance Act, 2020].**

The taxability in such cases shall be as under:

Domestic company receives dividend from another domestic company: The provisions of **section 80M** removes the cascading effect by providing that inter-corporate dividend shall be reduced from total income of company receiving the dividend if same is further distributed to shareholders one month prior to the due date of filing of return of Income.

| Section 80M | Deduction in respect of certain Inter Corporate Dividend (ICD) |
|----------------------------------|---|
| Meaning of ICD | When a company receives dividend by virtue of its shareholding in another company is known as ICD. |
| Applicability | To domestic companies who have declared dividend and are also in receipt of the dividend from another domestic company. |
| Coverage (Period) | Dividend distributed on or after the 1st of April 2020 (AY 2021-22 onwards). |
| Amount of Deduction (Rs.) | A. Amount of dividend received from domestic companies |
| | B. Amount of dividend distributed 1 month prior to the due date of filing return |
| | Amount of Deduction = A or B Whichever is lower |

CASE 1

DP Ltd (A Domestic Company) provides you the information related to AY: 2026-27. Dividend received from ACC Ltd. (A Domestic Company) Rs. 12,00,000 (Interest paid for borrowed money for investment in ACC Ltd Rs. 3,00,000 and dividend collection charges paid would be Rs. 7,000). Income from Mutual Fund (HDFC Equity Oriented) Rs. 3,00,000 (Interest paid for borrowed money for investment in MF Rs. 16,000 and other charges paid would be Rs. 4,000). DP Ltd company has distributed the dividend to shareholders:

| Particulars | FY | Date of Payment | Amount |
|------------------|---------|-----------------|----------|
| Interim Dividend | 2025-26 | 23-07-2025 | 2,50,000 |
| Interim Dividend | 2025-26 | 29-11-2026 | 90,000 |

You are required to compute Taxable Dividend Income and Deduction under section 80M and Section 57 of Income Tax Act.

Solution:**Computation of Taxable Dividend Income and deduction u/s 57**

| Particulars | | Amount |
|--|----------|-----------------|
| Dividend received from ACC ltd | | 12,00,000 |
| Less: Deduction u/s 57 in terms of Interest | | |
| (a) Actual Amount | 3,00,000 | |
| (b) 20% of income (i.e. 20% of 12,00,000) | 2,40,000 | |
| a or b whichever is lower | | (2,40,000) |
| Dividend income received | | 9,60,000 |
| Income from Mutual Fund (HDFC Equity oriented) | | 3,00,000 |
| Less: Deduction u/s 57 in terms of Interest | | |
| (a) Actual Amount | 16,000 | |
| (b) 20% of income (i.e. 20% of 3,00,000) | 60,000 | |
| a or b whichever is lower | | (16,000) |
| Income received | | 2,84,000 |

Computation of Deduction u/s 80M

| | |
|--|------------|
| Due date of filling of return | 30.09.2025 |
| (a) Amount of dividend received from domestic companies (As per above) | 9,60,000 |
| (b) Amount of dividend distributed 1 month prior to the due date of filing return (i.e. 30-9-2025) | 2,50,000 |
| Amount of Deduction u/s 80M = A or B Whichever is lower | 2,50,000 |

Note: Dividend collection charges and other charges are not allowed as a deduction.

Exemption for inter-corporate dividend distribution within IFSC Units engaged in the aircraft leasing business [Section 10(34B)]

The Finance Act 2023 has introduced a new clause (34B) in Section 10 of the Act, which will come into effect from the assessment year 2025-26. This clause exempts dividend income earned by an IFSC unit primarily engaged in aircraft leasing business. However, the exemption is subject to the condition that the company paying the dividend should also be an IFSC unit and engaged in the aircraft leasing business.

Taxability of Dividend in hands of Recipient

Section 10(34), which provides an exemption to the shareholders in respect of dividend income, **is withdrawn from Assessment Year 2021-22**. Thus, dividend received during the financial year 2020-21 and onwards shall now be taxable in the hands of the shareholders. Consequently, Section 115BBDA which provides for taxability of dividend in excess of Rs. 10 lakhs have no relevance as the entire amount of dividend shall be taxable in the hands of the shareholder.

The taxability of dividend and tax rate thereon shall depend upon many factors like residential status of the shareholders, relevant head of income. In case of a non-resident shareholder, the provisions of Double Taxation Avoidance Agreements (DTAAs) and Multilateral Instrument (MLI) shall also come into play.

Taxable in the hands of Resident Shareholder

Dividend income is taxable under the head 'Income from other sources' irrespective of fact that person held securities either as a trader or as an investor.

The assessee can claim deduction of only interest expenditure which has been incurred to earn that dividend income to the extent of 20% of total dividend income. No deduction shall be allowed for any other expenses including commission or remuneration paid to a banker or any other person for the purpose of realizing such dividend.

The dividend income shall be chargeable to tax at normal tax rates as applicable in case of an assessee except where a resident individual, being an employee of an Indian company or its subsidiary engaged in Information technology, entertainment, pharmaceutical or bio-technology industry, receives dividend in respect of GDRs issued by such company under an Employees' Stock Option Scheme. In such a case, dividend shall be taxable at concessional tax rate of 10% without providing for any deduction under the Income-tax Act. However, the GDRs should be purchased by the employee in foreign currency.

Taxability in case of non-resident shareholders including FPIs

A non-resident generally invests in India either directly as private equity investors or as Foreign Portfolio Investors (FPIs). A non-resident person can also be a promoter of an Indian Company. A non-resident person generally holds shares of an Indian company as an investment and, therefore, any income derived by way of dividend is taxable under the head other sources.

As regards FPIs, securities held by them are always treated as a capital asset and not as stock-in-trade. Thus, in case of FPIs also, the dividend income shall always be taxable under the head other sources.

The dividend income, in the hands of a non-resident person (including FPIs and non-resident Indian citizens (NRIs)), is taxable at the rate of 20% without providing for deduction under any provisions of the Income-tax Act. However, dividend income of an investment division of an offshore banking unit shall be taxable at the rate of 10%.

If the withholding tax rate as per DTAA is lower than the rate prescribed under the Finance Act then tax shall be deducted at the rate prescribed under DTAA.

BUY BACK OF SHARES

Special provisions relating to Tax on Distributed Income of Domestic Company for Buy -Back of Shares

The Finance Act (No. 2), 2024, effective from October 1, 2024, introduces significant changes to the tax implications in case of share buybacks of shares by domestic companies. Previously, under Section 115QA of the Income Tax Act, companies faced an additional tax liability of 20% plus applicable surcharges and education cess, resulting in an effective tax rate of 23.296% on the buyback of their shares. However, with the

new amendments, the tax burden has shifted from the company to the shareholders. **Now, payments made by a company for the buyback of its own shares will be treated as dividend income, as specified in the newly added clause (f) of Section 2(22). This change means shareholders will now be taxed on these proceeds as income from other sources.** The amendment also includes a new proviso to Section 115QA, stating that its provisions will not apply to buybacks occurring on or after October 1, 2024. Consequently, companies will be responsible for deducting tax at source (TDS) at a rate of 10% for resident shareholders and at applicable rates for non-residents. Additionally, shareholders can treat the cost of shares as a capital loss, which may be carried forward for eight subsequent financial years.

Tax Implication of Buy Back of Shares

Finance Act, 2024 has provided that w.e.f 01.10.2024, following changes will be made:

| Existing (upto 30.09.2024) | Amended (01.10.2024 Onwards) |
|---|---|
| Domestic Company buying back were liable to pay DDT/CDT on Distributed Income to shareholders u/s 115QA @ 23.296% (20% + 12% Surcharge + 4% HEC) within 14 Days of payment to Shareholders In case of Non-Payment of Tax u/s 115QA within 14 days, Interest @ 1% p.m. or part of month thereof was applicable from 15th day onwards. | Companies are not liable to pay tax on buyback u/s 115QA. Company is liable to deduct TDS u/s 194 w.e.f. 01.10.2024 |
| Shareholders were not required to pay any tax on amount received against buy back of shares from Domestic Company as per exemption u/s 10(34). Shareholders were required to pay any tax on amount received against buy back of shares from any company other than Domestic Company as per Section 46A. | Shareholders are liable to tax at Normal Rates and are required to treat the entire amount received under buy back as "Income from Other Sources" u/s 2(22)(f). No Deduction u/s 57 allowed on such income. Section 46A not applicable. |
| Cost of shares (to shareholders) which has been bought back will not be considered at all in any calculation of income. | Cost of shares (to shareholders) which has been bought back will be treated as long / short term capital loss, depending upon period of holding. |

(*Amendments w.e.f. 01.10.2024 – Section 115QA, 115QB, 10(34A), 2(22)(f), 46A, 194)

The above can be understood with help of below example:

Example: X Ltd balance sheet as on 31st March XXXX is as below:

| Liabilities | Amount | Assets | Amount |
|--|-----------|--------------|-----------|
| Equity Share Capital (1,20,000 shares of Rs 10 each) | 12,00,000 | Machinery | 10,00,000 |
| Securities Premium | 3,00,000 | Other Assets | 8,00,000 |
| Retained Earnings | 5,00,000 | Bank | 2,00,000 |
| Total | 20,00,000 | Total | 20,00,000 |

The cost of each share for shareholder was Rs 11 per share (assumed). Company decided to buy-back its 20,000 shares and agreed to pay (a) Rs 1 Lacs, (b) Rs 2 Lacs, (c) Rs 3 Lacs, (d) Rs 4 Lacs,

What will be tax treatment in the hands of shareholder receiving this consideration and in hands of the company.

Solution:

The cost of shares proposed to be bought back is Rs 2,20,000 (20,000 x 11). w.e.f. 01.10.2024, calculation of capital gain in hands of shareholder is as below:

| S. No. | Particulars | Case (a) | Case (b) | Case (c) | Case (d) |
|--------|---|-----------|-----------|-----------|-----------|
| A | Proceeds received on buyback by shareholder | 1,00,000 | 2,00,000 | 3,00,000 | 4,00,000 |
| | Income from other Sources | 1,00,000 | 2,00,000 | 3,00,000 | 4,00,000 |
| B | Cost of acquisition for the shareholder | 2,20,000 | 2,20,000 | 2,20,000 | 2,20,000 |
| | Capital (Loss) | -2,20,000 | -2,20,000 | -2,20,000 | -2,20,000 |

In the hands of Company which has bought-back shares there will be no requirement of paying Tax on distributed income on buy-back u/s 115QA.

Now w.e.f. 01/10/2024, Finance Act (No. 2) shifted the burden of tax payment from domestic company to the shareholder as the payment received by the shareholder will consider as dividend income and taxable in the hands of shareholder. Accordingly, new clause (f) inserted after clause (e) in section 2(22) in the definition of dividend, which are stated below: [(f) any payment by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 68 of the Companies Act, 2013 (18 of 2013);

SLUMP SALE

Section 2 (42C) of the Income Tax Act, 1961 “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.

“Undertaking” shall have the meaning assigned to it in Explanation 1 to clause (19AA).

The determination of the 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.

Understanding of provisions with regard to Slump Sale

For sale to be constituted as Slump Sale, following conditions must be satisfied –

- There must be sale of one or more undertakings,
- Sale must be for lump sum consideration and not in part or in installments,
- There must not be values assigned to individual assets and liabilities,

- For determination of the 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,
- The undertaking must be sold as going concern
- There must be an undertaking owned by the assessee,
- When one or more undertaking is transferred, then there has to be transfer of assets as well as liabilities, if only assets are transferred and not the liability then the same will not amount to slump sale

Special provision for computation of Capital Gains in case of Slump Sale [Section 50B]

Any profits or gains arising from the slump sale effected in the previous year shall be chargeable to income-tax as capital gains arising from the transfer of long-term capital assets and shall be deemed to be the income of the previous year in which the transfer took place.

Provided that any profits or gains arising from the transfer under the slump sale of any capital asset being one or more undertakings owned and held by an assessee for not more than thirty-six months immediately preceding the date of its transfer shall be deemed to be the capital gains arising from the transfer of short-term capital assets.

In relation to capital assets being an undertaking or division transferred by way of such sale, the “net worth” of the undertaking or the division, as the case may be, shall be deemed to be the cost of acquisition and the cost of improvement for the purposes of sections 48 and 49 and no regard shall be given to the provisions contained in the second proviso to section 48.

Every assessee, in the case of slump sale, shall furnish in the prescribed form 83 along with the return of income, a report of an accountant as defined in the Explanation below sub-section (2) of section 288, indicating the computation of the net worth of the undertaking or division, as the case may be, and certifying that the net worth of the undertaking or division, as the case may be, has been correctly arrived at in accordance with the provisions of this section.

The Bombay High Court while dealing with the concept of ‘slump sale’ generally clarified that one of the principle tests for determination of whether a transaction would be a ‘slump sale’ is whether there is continuity of business. Thus, the concept of ‘going concern’ is one of the most important conditions to be satisfied when analyzing whether a transaction can be regarded as a slump sale.

Explanation 1: “Net worth” shall be the aggregate value of total assets of the undertaking or division as reduced by the value of liabilities of such undertaking or division as appearing in its books of account.

Provided that any change in the value of assets on account of revaluation of assets shall be ignored for the purposes of computing the net worth.

Explanation 2: For computing the net worth, the aggregate value of total assets shall be:

- (a) in the case of depreciable assets, the written down value of the block of assets determined in accordance with the provisions contained in sub-item (C) of item (i) of sub-clause (c) of clause (6) of section 43;
- (b) in the case of capital assets in respect of which the whole of the expenditure has been allowed or is allowable as a deduction under section 35AD, Nil; and
- (c) in the case of other assets, the book value of such assets.

Related Rule(s)**Form of report of an accountant under sub-section (3) of section 50B**

The report of an accountant which is required to be furnished by every assessee before the specified date referred to in section 44AB” in case of slump sale, under sub-section (3) of section 50B shall be in Form No. 3CEA.

Related Form(s)

Form No. 3CEA - Report of an accountant to be furnished by an assessee under sub-section (3) of section 50B of the Income -tax Act, 1961 relating to computation of capital gains in case of slump sale.

SLUMP SALE AND CAPITAL GAIN TAX

When Slump Sale take place, there will be capital gain tax attracted and this is covered by Section 50B of the Income Tax Act, 1961. Let us understand this provisions in detail –

- Whenever there is a profit or gain due to slump sale, it will be deemed to be income of that particular year,
- Capital gain tax payable in case of slump sale can be divided into –
 - a. Capital gain arising from transfer of short-term capital assets – Capital assets being one or more undertakings owned and held by an assessee for not more than thirty-six months immediately preceding the date of its transfer shall be deemed to be the capital gains arising from the transfer of short-term capital assets and
 - b. Capital gain arising from transfer of long-term capital assets – Capital assets being one or more undertakings owned and held by an assessee for more than thirty-six months immediately preceding the date of its transfer shall be deemed to be the capital gains arising from the transfer of long-term capital assets
- Capital Assets may be divided into –
 - a. Depreciable assets,
 - b. Assets in respect of which the whole of the expenditure has been allowed or is allowable as a deduction under section 35AD and
 - c. Other assets
- Determination of “Net Worth” is an important part in case of determination of liability for purpose of Income Tax, Net worth of the undertaking or the division shall be -
 - a. Cost of acquisition and the cost of improvement,
 - b. Aggregate value of total assets of the undertaking or division as reduced by the value of liabilities of such undertaking or division as appearing in its books of account,

Further any change in the value of assets on account of revaluation of assets shall be ignored for the purposes of computing the net worth.

Calculation of “Net Worth” is a very important part for determining capital gain tax payable because tax payable is difference between sale consideration and the net worth of the undertaking.

- Computation for determining amount of tax payable shall be done separately for each sale of undertaking or more undertakings as the case may be,
- One of the major benefits which is taken away by Section 50B is that indexation benefit is not available in case of slump sale,

- Section 50B is a special provision for purpose of computation of capital gain in case of slump sale thus this section overrides all the provisions of the Income Tax Act, 1961 because specific provisions overrides general provision. This particular provision is specifically for computation of capital gain in case of slump sale.

CASE LAWS

In case of CIT vs. Equinox Solution Pvt. Ltd (Supreme Court) it was held that Section 45 and 50(2): If an undertaking is sold as a running business with all assets and liabilities for a slump price, no part of the consideration can be attributed to depreciable assets and assessed as a short-term capital gain u/s 50(2). If the undertaking is held for more than three years, it constitutes a “long-term capital asset” and the gains are assessable as a long-term capital gain.

Example -1

ABC Limited, a public company incorporated under the Companies Act, has two units – one engaged in manufacture and the other involved in service. As the company is planning restructuring of the company, it has decided to sell its service unit as a going concern by way of slump sale for Rs. 38,500 to a new company called XYZ Limited, in which it holds 74% equity shares.

The balance sheet of ABC limited as on 31st March 2026, being the date on which service unit has been transferred, is given hereunder –

Balance sheet as on 31.03.2026

| Liabilities | Amount in Rs. | Assets | Amount in Rs. |
|----------------------------|---------------|---------------------|---------------|
| Paid up Share Capital | 30,000 | Fixed Assets | |
| General Reserve | 15,000 | Manufacturing Unit | 17,000 |
| Share Premium | 5,000 | Service Unit | 20,000 |
| Revaluation Reserve | 12,000 | Debtors | |
| Current Liabilities | | Manufacturing Unit | 14,000 |
| Manufacturing Unit | 4,000 | Service Unit | 11,000 |
| Service Unit | 9,000 | Inventories | |
| | | Manufacturing Unit | 9,500 |
| | | Service Unit | 3,500 |
| Total | 75,000 | Total | 75,000 |

Company has furnished following additional information -

- The Service unit is in existence since May, 2019.
- Fixed assets of Service unit include land which was purchased at Rs. 4,000 in the year 2016 and revalued at Rs. 6,000 as on March 31, 2026.
- Fixed assets of Service unit are at Rs. 14,000 (Rs. 20,000 minus land value Rs.6,000) is written down value of depreciable assets as per books of account. However, the written down value of these assets under section 43(6) of the Income-tax Act is Rs.9,000.

Ascertain the tax liability, which would arise from slump sale to ABC Limited.

Answer:

- Capital Gains = “Slump sale consideration” **minus** “Net worth of the Undertaking or division”
- “Net worth” = Aggregate value of total assets of the undertaking or division transferred **minus** Value of Liabilities of the undertaking or division transferred as appearing in its books of account.
- For computing the “net worth”, non-depreciable assets are to be taken at their book values and in case of depreciable assets, the written down value of such assets shall be computed as per section 43(6)(c).

In the present case, the capital gains are long term since period of holding of software unit shall be from May 2019 to March 2026.

Computation of Net Worth of Service Unit-

| Particulars | Amount in Rs. |
|--|---------------|
| Depreciable assets (W.D.V. as per Income Tax Act) | 9,000 |
| Land | 4,000 |
| Debtors | 11,000 |
| Inventory | 3,500 |
| Total assets | 27,500 |
| Less: Current liability | 9,000 |
| Net worth | 18,500 |
| Computation of capital gain on transfer of service unit – | |
| Full value of sale consideration | 38,500 |
| Less: Net worth of service unit | 18,500 |
| Long Term capital gain | 20,000 |

ISSUE OF SHARES AT PREMIUM**Relevant provision of Section 56 with regard to Share Premium Amount**

Section 56(2)(viib) was introduced in 2012 as Angel Tax, to curb the unaccounted black money in circulation, w.r.t., companies being closely held Indian Companies receiving any consideration on issue of shares (equity or preference)

Section 56(2)(viib) of the Act, reads as follows -

- (viib) where a company, not being a company in which the public are substantially interested, receives in any previous year, from any person, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares:

Provided that this clause shall not apply where the consideration for issue of shares is received –

- (i) by a venture capital undertaking from a venture capital company or a venture capital fund or specified fund; or

- (ii) By a startup recognised by DPIIT with conditions; or
- (iii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.

Provided further that where the provisions of this clause have not been applied to a company on account of fulfilment of conditions specified in the notification issued under clause (ii) of the first proviso and such company fails to comply with any of those conditions, then, any consideration received for issue of share that exceeds the face value of such share shall be deemed to be the income of that company chargeable to income-tax for the previous year in which such failure has taken place.

Further, this section is not applicable to 'startup', CBDT has referred to 'startups' as defined in the notification issued in February 2019 by Department of Industrial Policy and Promotion ('DIPP'), whereby an entity shall be considered as a 'startup'. This exemption is available up to 5 years from its date of incorporation / registration and if it is a private limited company.

For concessional share allotment at less than book value (under rule 11U & 11UA) held bonus shares do not fall under the same; right shares and original first-time allotment falls in the same however if new shares allotted to existing shareholders pro rata as per exiting holdings no adverse inference/addition possible.

Important part as far as this section is concerned is determination of fair market value of shares, this is determined as below –

$$(a) \text{ the fair market value of unquoted equity shares} = \frac{(A-L)}{(PE)} \times (PV),$$

where,

A = book value of the assets in the balance-sheet as reduced by any amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax Act and any amount shown in the balance-sheet as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset;

L = book value of liabilities shown in the balance-sheet, but not including the following amounts, namely:—

- (i) the paid-up capital in respect of equity shares;
- (ii) the amount set apart for payment of dividends on preference shares and equity shares where such dividends have not been declared before the date of transfer at a general body meeting of the company;
- (iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation;
- (iv) any amount representing provision for taxation, other than amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax Act, to the extent of the excess over the tax payable with reference to the book profits in accordance with the law applicable thereto;
- (v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;
- (vi) any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares;

PE = total amount of paid up equity share capital as shown in the balance-sheet; PV = the paid up value of such equity shares; or

Explanation: For the purposes Section 56(2)(viib)

- (a) Fair market value of the shares shall be the value—
 - (i) as may be determined in accordance with such method as may be prescribed; or
 - (ii) as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature,

whichever is higher;

- (aa) “specified fund” means a fund established or incorporated in India in the form of a trust or a company or a limited liability partnership or a body corporate which has been granted a certificate of registration as a Category II Alternative Investment Fund and is regulated under the Securities and Exchange Board of India (Alternative Investment Fund) Regulations, 2012 made under the Securities and Exchange Board of India Act, 1992 [Inserted by Finance Act, 2019]
- (ab) “trust” means a trust established under the Indian Trusts Act, 1882 or under any other law for the time being in force; [Inserted by Finance Act, 2019]
- (b) “Venture capital company”, “Venture capital fund” and “Venture capital undertaking” shall have the meanings respectively assigned to them in clause (a), clause (b) and clause (c) of Explanation to Section 10(23FB);

“unquoted shares and securities” means shares and securities which is not a quoted shares or securities;

“merchant banker” means category I merchant banker registered with the Securities Exchange Board of India established under section 3 of the Securities Exchange Board of India Act, 1992 (15 of 1992)

“balance-sheet” in relation to any company means the balance-sheet of such company (including the notes annexed thereto and forming part of the accounts) as drawn up on the valuation date which has been audited by the auditor of the company appointed under Companies Act and where the balance-sheet on the valuation date is not drawn up, the balance-sheet (including the notes annexed thereto and forming part of the accounts) drawn up as on a date immediately preceding the valuation date which has been approved and adopted in the annual general meeting of the shareholders of the company

“valuation date” means the date on which the property or consideration as the case may be, is received by the assessee.

“Share premium” is the amount by which the issue price of a share exceeds the nominal value and under the Companies Act, the value of the share premium must be credited to a securities premium account.

This section is applicable only to closely held companies and not to companies in which public is substantially interested. Income Tax Act does not define closely held companies but Section 2(18) of the Income Tax Act, 1961 defines ‘a company in which the public is substantially interested’ to include :-

- a. a company owned by the Government or the RBI or more than forty percent of the shares are owned by Government or the RBI or a corporation owned by the RBI.
- b. a company registered under section 25 of the Companies Act, 1956.
- c. a company not having share capital and declared by the Board to be such company
- d. Mutual Benefit Finance Company – business of acceptance of deposits from members and notified by the Central Government u/s 620 of the Companies Act, 1956.

- e. a company, whose more than 50% Equity Shares (not being Preference Shares) held by one or more Co-operative Societies throughout the previous year.
- f. a company not being a Private Company as defined in the Companies Act, 1956, whose Equity Shares were listed on the 31 March of the previous year in a Recognised Stock Exchange.
- g. a 'Government Company' not being a 'Private Company'.

The Section 56(2)(viib) does not distinguish between an Indian or a Foreign Company. Section 2(17) defines "company" to include a body corporate incorporated by or under the laws of a country outside India.

Note: Abolition of Angel Tax: The Finance Act, 2024, abolished Section 56(2)(viib). This marked a significant policy shift aimed at boosting the startup ecosystem and reducing regulatory hurdles for fundraising. The provisions of this clause shall not apply on or after the 1st day of April, 2025. [As amended by Third Proviso to Section 56(2)(viib)].

CASE LAWS

In case of Vodafone India Services Private Limited v. Union of India [2014] 50 taxmann.com 300 (Bombay HC) it was held that the issue of shares at a premium by the company to its non-resident holding company does not give rise to any income from an admitted International Transaction. Thus, no occasion to apply Chapter X of the Act can arise in such a case.

Example –

ABC Private Limited is a closely held company, its board of directors decided to issue 500 shares face value of which is Rs. 100 per share, fair market value of which is Rs. 150 per share at a premium of Rs. 200 per share. Please advise whether section 56 will be attracted and tax payable, in following circumstances –

In case the investor/subscribers to the shares of above-named company are

- a. Resident Indian,
- b. Non-resident Indian,
- c. Venture Capital undertaking.

Further, what will be your answer, if the shares are issued at fair market value.

Answer:

In case the investors/subscribers are Resident Indian than tax liability will be issue price Rs. 300 (i.e. Rs. 100 face value plus Rs. 200 share premium) minus Rs. 150 (fair market price) = Rs. 150 per share. Total tax needs to be paid on Rs. 75,000/-.

In case the investors/subscribers are non-resident Indian and venture capital undertaking than no tax liability has they are exempted under Section 56 of the Act.

In case the shares were issued at fair market value instead at face value or at premium than no tax liability would have occurred.

TRANSFER OF SHARES**Special provision for full value of consideration for transfer of share other than quoted share [Section 50CA]**

Where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being share of a company other than a quoted share, is less than the fair market value of such share determined in such manner as may be prescribed, the value so determined shall, for the purposes of section 48, be deemed to be the full value of consideration received or accruing as a result of such transfer.

Provided that the provisions of this section shall not apply to any consideration received or accruing as a result of transfer by such class of persons and subject to such conditions as may be prescribed.

Explanation: For the purposes of this section, “quoted share” means the share quoted on any recognised stock exchange with regularity from time to time, where the quotation of such share is based on current transaction made in the ordinary course of business.

Example 1: Mr. Ram is working in a company and has salary income. In the month of June, 2025 he purchased equity shares of ABC India Limited which is listed on BSE and sold the same in January, 2026. In this case shares are capital assets for Mr. Ram. He purchased shares in June, 2025 and sold them in January, 2026, i.e., after holding them for a period of less than 12 months.

Hence, shares will be treated as Short Term Capital Assets.

In case Mr. Ram had sold the shares in the month of September, 2026 i.e., after holding them for a period of more than 12 months. Then in this case it will be treated as Long Term Capital Assets.

Section 111A is applicable in case of STCG arising on transfer of equity shares or units of equity oriented mutual-funds or units of business trust which are transferred on or after 1-10-2004 through a recognised stock exchange and such transaction is liable to securities transaction tax.

If the conditions of section 111A are satisfied then the STCG charged to Tax at Special Concessional Rates under section 111A. Such gain is charged to tax at 15% or 20% (plus surcharge and HEC as applicable).

| Date of Transfer | Concessional Tax Rate (Special Rates) |
|--|---------------------------------------|
| Up to 22.07.2024 (Prior to 23.07.2024) | 15% |
| On or After 23.07.2024 | 20% |

Example 2: Mr. D is in employment. In the month September, 2023 he had purchased unlisted shares of XYZ Limited and sold the same in May 2025. In this case, shares are sold in assessment year 2026-27. Hence, period of holding for unlisted shares to be considered as 24 months.

Mr. D purchased shares in September 2023 and sold it on May 2025, i.e., after holding them for a period of less than 24 months. Hence, shares will be treated as Short Term Capital Assets.

Mode of Computation [Section 48]

The income chargeable under the head “Capital gains” shall be computed, by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts:

- (i) expenditure incurred wholly and exclusively in connection with such transfer;
- (ii) the cost of acquisition of the asset and the cost of any improvement thereto:

Provided that in the case of an assessee, who is a non-resident, capital gains arising from the transfer of a capital asset being shares in, or debentures of, an Indian company shall be computed by converting the cost of acquisition, expenditure incurred wholly and exclusively in connection with such transfer and the full value of the consideration received or accruing as a result of the transfer of the capital asset into the same foreign currency as was initially utilised in the purchase of the shares or debentures, and the capital gains so computed in such foreign currency shall be reconverted into Indian currency, so, however, that the aforesaid manner of computation of capital gains shall be applicable in respect of capital gains accruing or arising from every reinvestment thereafter in, and sale of, shares in, or debentures of, an Indian company :

Provided further that where long-term capital gain arises from the transfer (which takes place before the 23rd day of July, 2024) of a long-term capital asset, other than capital gain arising to a non-resident from the transfer of shares in, or debentures of, an Indian company referred to in the first proviso, the provisions of clause (ii) shall have effect as if for the words “cost of acquisition” and “cost of any improvement”, the words “indexed cost of acquisition” and “indexed cost of any improvement” had respectively been substituted:

Provided also that nothing contained in the first and second provisos shall apply to the capital gains arising from the transfer of a long-term capital asset being an equity share in a company or a unit of an equity-oriented fund or a unit of a business trust referred to in section 112A.

Provided also that nothing contained in the second proviso shall apply to the long-term capital gain arising from the transfer of a long-term capital asset, being a bond or debenture other than:

- (a) capital indexed bonds issued by the Government; or
- (b) Sovereign Gold Bond issued by the Reserve Bank of India under the Sovereign Gold Bond Scheme, 2015:

Provided also that in case of an assessee being a non-resident, any gains arising on account of appreciation of rupee against a foreign currency at the time of redemption of rupee denominated bond of an Indian company held by him, shall be ignored for the purposes of computation of full value of consideration under this section:]

Provided also that where shares, debentures or warrants referred to in the proviso to clause (iii) of section 47 are transferred under a gift or an irrevocable trust, the market value on the date of such transfer shall be deemed to be the full value of consideration received or accruing as a result of transfer for the purposes of this section:

Provided also that no deduction shall be allowed in computing the income chargeable under the head “Capital gains” in respect of any sum paid on account of securities transaction tax under Chapter VII of the Finance (No. 2) Act, 2004.

[Rule 115A] read with 1st Proviso to Section 48

For the purpose of computing capital gains arising from the transfer of a capital asset being shares in, or debentures of, an Indian company, in the case of an assessee who is a non-resident Indian, the rate of exchange shall be:

- (a) for converting the cost of acquisition of the capital asset, the average of the telegraphic transfer buying rate and telegraphic transfer selling rate of the foreign currency initially utilised in the purchase of the said asset, as on the date of its acquisition;
- (b) for converting expenditure incurred wholly and exclusively in connection with the transfer of the capital asset referred to in clause (a), the average of the telegraphic transfer buying rate and telegraphic transfer selling rate of the foreign currency initially utilised in the purchase of the said asset, as on the date of transfer of the capital asset;

- (c) for converting the full value of consideration received or accruing as a result of the transfer of the capital asset referred to in clause (a), the average of the telegraphic transfer buying rate and telegraphic transfer selling rate of the foreign currency initially utilised in the purchase of the said asset, as on the date of transfer of the capital asset;
- (d) for reconverting capital gains computed in the foreign currency initially utilised in the purchase of the capital asset into rupees, the telegraphic transfer buying rate of such currency, as on the date of transfer of the capital asset.

Explanation: For the purposes of this rule:

- (i) “telegraphic transfer buying rate” shall have the same meaning as in the Explanation to rule 26;
- (ii) “telegraphic transfer selling rate”, in relation to a foreign currency, means the rate of exchange adopted by the State Bank of India constituted under the State Bank of India Act, 1955, for selling such currency where such currency is made available by that bank through telegraphic transfer.]

REDUCTION OF SHARE CAPITAL

Under the provisions of the Companies Act, 2013 and rules made thereunder, a company may go for reduction of share capital in any of the following manner –

- a. Extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or
- b. Either with or without extinguishing or reducing liability on any of its shares,
 - (i) cancel any paid-up share capital which is lost or is unrepresented by available assets; or
 - (ii) pay off any paid-up share capital which is in excess of the wants of the company, alter its memorandum by reducing the amount of its share capital and of its shares accordingly
- c. Buy Back of Shares.
- d. In case the securities premium account is applied by the company except on following –
 - (a) towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares;
 - (b) in writing off the preliminary expenses of the company;
 - (c) in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company;
 - (d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company; or
 - (e) for the purchase of its own shares or other securities under section 68.

Section 2(22)(d) of the Income Tax Act, 1961 exclusively deals with deemed dividend arising in the event of reduction of share capital. It states that any distribution to its shareholders by a company on the reduction of its capital, to the extent to which the company possesses accumulated profits whether such accumulated profits have been capitalised or not. It thus seeks to tax distribution of accumulated profits under the guise of returning/reducing capital.

When a company has an excess of accumulated profits over and above its requirement, it may use such accumulated profits to reduce its share capital instead of capitalising it. In other words, the company may, out of its accumulated profits, pay off any share capital which is in excess of what it wants. In such cases there is evidently a release of assets.

Any such distribution by a company on reduction of its capital is 'dividend' to the extent to which the company possesses accumulated profits whether capitalised or not.

However, where the reduction is greater than the accumulated profits, then it is a case of genuine reduction of capital. Any capital so returned is genuinely a capital receipt in the hands of the shareholders and is accordingly exempt from tax.

Section 56 states that dividend income is chargeable to tax under the head 'Income from Other Sources' (IFOS). In the case of CIT v Jai Hind Investment Industries (P) Ltd (1993) 202 ITR 316 (Cal) it is stated that when the amount paid by the company has been treated as dividend, there is no scope for reduction of face value of shares from such dividend.

Further, section 57 additionally states that the only deduction allowable from such dividend income is the interest expense to the extent of 20% of the total dividend income.

Capital Gain Tax

In *Kartikeya V. Sarabhai v CIT* (1997) Supreme Court it was held that reduction of share capital by a company and paying off the balance to the shareholders would result in extinguishment of rights in the shares held by the shareholder and would amount to transfer. On reduction of share capital, the rights of the shareholders in the dividend and net assets are extinguished. Therefore, capital gains would arise.

In *G. Narasimham* (Supreme Court) 1998, it was held that the amount distributed by the company on reduction of its share capital has two components, namely:

- a. Distribution attributable to accumulated profits and
- b. Distribution attributable to the capital

The Supreme Court held that out of the amount received on reduction of share capital, the amount attributable to accumulated profits will be deemed as dividend u/s 2(22)(d) and balance amount is the sale proceeds of the shares so reduced.

Conclusion

In simple words, the income of the shareholder, in the event of reduction of share capital by a company, is to be computed as follows:

| Particulars | Amount |
|---|-----------------|
| Fair Market Value of assets received (if any) | Rs. xxx |
| Add: Cash received | Rs. xxx |
| Total amount received on reduction of capital | Rs. xxx |
| Less: Deemed Dividend u/s 2(22)(d) | Rs. xxx |
| Sale Proceeds of the shares so reduced | Rs. xxx |
| Less: Cost of Acquisition of the shares held | Rs. xxx |
| Capital Gains / Loss (Long Term / Short Term) | Rs. xxx / (xxx) |

The taxation of the above incomes is as follows:

| Particulars | Head | Tax Rates |
|---------------------------------|------|----------------------------------|
| Deemed Dividend u/s 2(22)(d) | IFOS | At normal rates |
| Long Term Capital Gains u/s 112 | CG | At Specified Rate of STCG / LTCG |

QUESTIONS FOR PRACTICE

Illustration 1

ABC Ltd. is engaged in manufacturing of chemicals and plastics since 1980. Depreciated value of block of asset (depreciation rate: 15%) on April 1, 2025 is Rs.15,00,000. The company purchased Plant X (rate of depreciation 15%) on June 15, 2025 for Rs. 4,18,000 (It is not eligible for additional depreciation). It is put to use on the same day. The company sold Plant Y (rate of depreciation 15%) on December 16, 2025 for (a) Rs. 11,70,000 (b) Rs. 14,70,000 (c) Rs. 25,70,000. The company transfers plastics division by way of slump sale on December 31, 2025 for Rs. 6.60 lakhs (expenditure on transfer: Rs. 1.60 lakhs). The following information in respect of plastics division is noted from the company's records and certified by the chartered accountant of the company in Form 3CEA –

| | |
|--|----------|
| Actual cost of assets acquired in 2016-17 | 6,40,000 |
| Depreciation claimed under the Income-tax Act upto AY 2017-18 | 60,000 |
| Depreciation that would have been allowable for the assessment years 2017-18 to 2025-26 as if the asset was the only asset in the relevant block | 90,000 |

Find out the amount of depreciation and capital gain chargeable to tax for the assessment year 2026-27.

Solution:

If Plant Y is transferred for

| Particular | Rs. 11.70 lakhs | Rs. 14.70 lakhs | Rs. 25.70 lakhs |
|---|-----------------|-----------------|-----------------|
| Depreciated value of the block of assets on April 1, 2025 | 15,00,000 | 15,00,000 | 15,00,000 |
| Add: Actual cost of Plant X acquired during the year | 4,18,000 | 4,18,000 | 4,18,000 |
| Less: Sale proceeds of Plant Y (it cannot exceed Rs. 15 lakhs + Rs. 4.18 lakhs) | 11,70,000 | 14,70,000 | 19,18,000 |
| Balance (a) | 7,48,000 | 4,48,000 | 0 |
| Less: Actual cost minus depreciation of assets of paper division transferred by way of slump sale [i.e. Rs. 6,40,000 – Rs. 60,000 – Rs. 90,000 = Rs. 4,90,000, it cannot however, exceed (a)] (b) | 4,90,000 | 4,48,000 | - |
| Written down value of the block on March 31, 2026 | 2,58,000 | Nil | Nil |
| Depreciation for the previous year 2025-26 @ 15% | 38,700 | Nil | Nil |
| Depreciated value of the block on April 1, 2026 | 2,19,300 | Nil | Nil |

| If Plant Y is transferred for | | | |
|---|-----------------|-----------------|-----------------|
| Capital gain on transfer of Plant Y as per section 50 | Rs. 11.70 lakhs | Rs. 14.70 lakhs | Rs. 25.70 lakhs |
| Sale consideration of Plant Y | N.A. | N.A. | 25,70,000 |
| Less: Cost of acquisition as per section 50 (i.e., Rs. 15 lakhs + Rs. 4.18 lakhs) | – | – | 19,18,000 |
| Less: Sale proceeds of Plant Y (it cannot exceed Rs. 15 lakhs + Rs. 4.18 lakhs) | 11,70,000 | 14,70,000 | 19,18,000 |
| Short term capital gain | – | – | 6,52,000 |
| Capital gain on transfer of depreciable assets of plastic division | | | |
| Sale proceeds | 6,60,000 | 6,60,000 | 6,60,000 |
| Less: Cost of acquisition and cost of improvement [being the net worth mentioned at (b)] (benefit of indexation is not available) | 4,90,000 | 4,48,000 | Nil |
| Expenses on transfer | 1,60,000 | 1,60,000 | 1,60,000 |
| Long term capital gain | 10,000 | 52,000 | 5,00,000 |

Illustration 2:

Z gets 1000 partly convertible debentures (face value Rs. 100) of A Ltd. (cost being Rs. 200 per debenture) at the time of original allotment to him on May 16, 2004. As per terms of allotment, A Ltd. converts 60 % portion of each debenture into 2 equity shares (Unlisted) of face value of Rs. 10 on July 1, 2012. On May 10, 2025, Z transfers 2000 equity shares in A Ltd. @ Rs. 600 per share and 1,000 (non-convertible portion) debentures @ Rs. 310 per debenture. Find out the amount of capital gains chargeable to tax for the assessment year 2026-27.

Solution: Immediately after conversion of debentures into equity shares, Z holds the following –

| No. of scrip | Type of scrip | Face value (per scrip) (Rs.) | Total cost (Rs.) |
|--------------|---------------|------------------------------|------------------|
| 2000 | Equity shares | 10 | 1,20,000* |
| 1000 | Debentures | 40 | 80,000** |
| Total | | | 2,00,000 |

*60% of original investment of Rs. 2,00,000 i.e. Rs. 1,20,000

**Rs. 2,00,000 – Rs. 1,20,000

Computation of Capital Gains

| Particulars | Debentures (Rs.) | Shares (Rs.) |
|---------------------------|------------------|--------------|
| Sale consideration | 3,10,000 | 12,00,000 |
| Less: Cost of Acquisition | 80,000 | 1,20,000 |
| Long term capital gains | 2,30,000 | 10,80,000 |

Illustration 3: A Ltd. has two undertaking X and Y. The following information is available.

| Particular | (Rs. in thousand) | | |
|--|-------------------|-------------------|-------|
| | Unit X | Unit Y | Total |
| Assets | | | |
| Rate of Depreciation | Plant R and S 15% | Plant P and Q 15% | |
| Depreciated value as on April 1, 2023 | - | 600 | 600 |
| Add: Actual cost of old plant R & S acquired on June 1, 2023 | 400 | - | 400 |
| Less: Sale proceed of plant P transferred on November 30, 2023 | - | 900 | 900 |
| Written down value on March 31, 2024 | 400 | - | 100 |
| Less: Depreciation 2023-24 | 60 | - | 15 |
| Depreciated Value on April 1, 2024 | 340 | - | 85 |
| Less: Depreciation on 2024-25 | 51 | - | 12.75 |
| Depreciated Value on April 1, 2025 | 289 | - | 72.25 |

On April 1, 2025, Unit X is transferred to B Ltd., an Indian company, in a scheme of de-merger. What will be written down value and actual cost in the hands of A Ltd. and B Ltd.?

Solution:

Written down value in the hands of A Ltd.

| | |
|---|----------|
| Depreciated value of assets on April 1, 2025: | 72,250 |
| Less: Written down value of assets transferred to B Ltd.: | 2,89,000 |
| Written down value on April 1, 2025 | Nil |

Note: by virtue of section 47(vib) income is not taxable under the head capital gains. Written down value in the hands of B Ltd. = Rs. 2,89,000

Illustration 4: Company X is proposed to be merged with company Y. The following are the particulars of the former company.

Unabsorbed depreciation: Rs. 2,50,65,000

Unabsorbed business losses: Rs. 1,15,10,000

Consider which of the benefit can be availed by company Y and advise the latter on the condition to be fulfilled to claim each such benefit.

Solution:

There is no indication in the question whether merger of company A and B satisfy conditions of section 2(1B) and 72A.

Answer to the given question can be given under following three situations:

- (a) If merger is not amalgamation within the meaning of section 2(1B) or
- (b) If merger is an amalgamation within the meaning of section 2(1B) but it does not fulfill the conditions of section 72A or
- (c) If merger satisfy conditions of section 2(1B) as well as 72A

Under the aforesaid situations, the position regarding the set off of unabsorbed loss/allowances by company B will be as under:

| Whether company Y can set off the unabsorbed loss/allowances of company X | Situation (a) | Situation (b) | Situation (c) |
|---|---------------|---------------|---------------|
| Unabsorbed depreciation of Rs. 2,50,65,000 | No | No | Yes |
| Unabsorbed business losses of Rs. 1,15,10,000 | No | No | Yes |

As is evident from the aforesaid chart, all unabsorbed business losses / allowances can be set off if the merger satisfies requirement of section 72A. Alternatively, in order to retain the advantage of claiming set-off of unabsorbed loss / allowances, the business of company Y may be taken over by Company X in that case, all unabsorbed loss / allowance can be set off by company X, even if the merger does not satisfy the condition of section 2(1B) and 72.

Illustration 5: Company A, which has an accumulated business loss of Rs. 5,00,000 and unabsorbed depreciation of Rs. 3,00,000 wants to reorganize its business by amalgamating with a rival company B, which is engaged in the same line of production but with a smaller capital, but has an efficient management set-up and more modern machinery. Company B is agreeable to the amalgamation.

What are the alternative courses available to the companies for effecting the merger and how would you advise them as to the best course of action?

Solution:

The alternative of merger that are available to company A and B are

- i) Merger of A into B, whereby A goes out of existence
- ii) Merger of B into A whereby B goes out of existence
- iii) Merger of A and B into a new company, whereby a new company say C, is formed and both A and B go out of existence.

All the three mergers can take place under one of the following situations.

- If merger is not amalgamation within the meaning of section 2(1B) or
- If merger is an amalgamation within the meaning of section 2(1B) but it does not fulfill the conditions of section 72A or
- If merger satisfy conditions of section 2(1B) as well as 72A

Under the aforesaid situations, the position regarding the set off of unabsorbed loss of Rs. 5,00,000 and unabsorbed depreciation of Rs. 3,00,000 will be as under:

| Whether set off the unabsorbed loss/ depreciation is possible | Situation (a) | Situation (b) | Situation (c) |
|--|---------------|---------------|---------------|
| Merger of A into B, whereby A goes out of existence | No | No | Yes |
| Merger of B into A whereby B goes out of existence | Yes | Yes | Yes |
| Merger of A and B into a new company, whereby a new company say C, is formed and both A and B go out of existence. | No | No | Yes |

To conclude, it can be said that the conditions of section 72A are satisfied, any of the three alternatives for mergers can be adopted as in all the cases the loss can be set off by the amalgamated company. However, if conditions of section 72A are not satisfied, alternative (ii) should be adopted as in this case, company A would be able to carry forward and set off of business loss and depreciation even if the merger does not satisfy the requirement of section 2(1B). This kind of merger also known as reverse merger.

CARBON CREDIT [SECTION 115BBG]

| | |
|-----------------------------------|--|
| Meaning of Carbon Credit | <ul style="list-style-type: none"> "carbon credit" in respect of one unit shall mean reduction of one tonne of carbon dioxide emissions or emissions of its equivalent gases which is validated by the United Nations Framework on Climate Change and which can be traded in market at its prevailing market price. It is a tradable permit or certificate to an industrial undertaking for reduction of the emission keeping in mind of global warming. |
| Coverage and Applicability | <ul style="list-style-type: none"> Where the total income of an assessee includes any income by way of transfer of carbon credits. |
| Tax Rate | <ul style="list-style-type: none"> Concessional rate of 10% (+SC+HEC) on the gross amount of such income. No expenditure or allowance in respect of such income shall be allowed. |

EQUALISATION LEVY

ABOLISHED w.e.f., 01.04.2025

In a significant policy development, the Government of India announced the abolition of the 6% Equalisation Levy on online advertisements, w.e.f., 1st April, 2025, following the earlier withdrawal of 2% Equalization Levy on e-commerce transactions in August 2024, marking a complete rollback of India's unilateral digital tax regime.

Up to 31.03.2025

With digital commerce continuing to transform the global economy, traditional tax frameworks have encountered major challenges to tackle tax leakages arising from cross-border digital transactions, which transformed global

value chains, enabling multinational companies to integrate operations across jurisdictions without a physical presence, posing major challenges to international taxation, leading to concerns over Base Erosion and Profit Shifting ('BEPS').

In response to these concerns, the Organization for Economic Co-operation and Development ('OECD'), in collaboration with G20, introduced 15 BEPS Action Plans.

Recognizing these challenges, India, introduced the Equalization Levy in 2016 as a unilateral measure to tax the payments made to non-resident entities for online advertising services at the rate of 6%. In 2020, the scope of the levy was expanded to include e-commerce transactions at the rate of 2%, thereby extending its reach to a broader spectrum of digital activities conducted by foreign companies without a physical presence in India.

Equalisation Levy was introduced in 2016 vide Section 165 to 172 of the Finance Act, 2016, aiming to target the rapid growth of the information and communication technology which resulted in substantial expansion of the supply and procurement of digital goods and services globally, including India, and the digital economy is growing at approximately 10% per annum, faster than the economy as a whole.

These new business models have brought along with themselves, challenges. The typical issues / concerns around taxation vis-à-vis e-commerce are:

- a) difficulty in characterizing the nature of payment and establishing a link / nexus between taxable transaction, activity and taxing jurisdiction.
- b) the difficulty in locating the transaction, activity and identifying the tax payer.

The Organization for Economic Cooperation and Development (OECD), has recommended several options to tackle these challenges.

Charge of equalisation levy on specified services [Section 165]

In order to address these challenges as stated above, Chapter VIII of the Finance Act, 2016 titled "Equalization Levy" provides for an equalization levy of 6% on the amount of consideration for specified services, received / receivable by a non- resident, not having permanent establishment in India, from a resident in India, who carries out business / profession, or from a non-resident who has a permanent establishment in India.

The equalisation levy shall not be charged in the following cases:

- (a) where the e-commerce operator making or providing or facilitating e-commerce supply or services has a permanent establishment in India and such e-commerce supply or services is effectively connected with such permanent establishment;
- (b) the aggregate amount of consideration for specified service received or receivable in a previous year by the non-resident from a person resident in India and carrying on business or profession, or from a non-resident having a permanent establishment in India, does not exceed one lakh rupees; or
- (c) where the payment for the specified service by the person resident in India, or the permanent establishment in India is not for the purposes of carrying out business or profession.

Note: The provisions of this section shall not apply to any consideration for any specified service received or receivable by a person on or after the 1st day of April, 2025. [Amendment vide Finance Act, 2025].

Charge of equalisation levy on e-commerce supply of services [Section 165A]

As amended by Finance Act, 2020, an equalization levy of 2% shall be charged on or after 01.04.2020 on the consideration by **an e-commerce operator** from e-commerce supply made or provided by it:

- (a) to a person resident in India;
- (b) to a non-resident in the specified circumstances as referred to in sub-section (3);
- (c) to a person who buys such goods or services or both using internet protocol address located in India.

Where e-commerce operator means a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both. E-commerce supply or services means-

- (i) online sale of goods owned by the e-commerce operator;
- (ii) online provision of services provided by the e-commerce operator;
- (iii) online sale of goods or provision of services or both, facilitated by the e-commerce operator;
- (iv) any combination of activities listed in clause (i), (ii) or clause (iii).

The equalisation levy shall not be charged on e-commerce operator -

- (i) where the e-commerce operator making or providing or facilitating e-commerce supply or services has a permanent establishment in India and such e-commerce supply or services is effectively connected with such permanent establishment;
- (ii) where the equalisation levy is leviable under section 165; or
- (iii) sales, turnover or gross receipts, as the case may be, of the e-commerce operator from the e-commerce supply or services made or provided or facilitated as referred to in sub-section (1) is less than two crore rupees during the previous year.

Note: The provisions of this section shall not apply to any consideration received or receivable by an e-commerce operator from e-commerce supply or services made or provided or facilitated by it on or after the 1st day of August, 2024. [Amendment vide Finance Act, 2024].

Collection and recovery of equalisation levy on specified services [Section 166]

Every person, being a resident and carrying on business or profession or a non-resident having a permanent establishment in India shall deduct the equalisation levy from the amount paid or payable to a non-resident in respect of the specified service at the rate specified, if the aggregate amount of consideration for specified service in a previous year exceeds one lakh rupees.

The equalisation levy so deducted during any calendar month shall be paid by every assessee to the credit of the Central Government by the seventh day of the month immediately following the said calendar month

Collection and recovery of equalisation levy on e-commerce supply or services [Section 166A]

The equalisation levy, shall be paid by every e-commerce operator to the credit of the Central Government for the quarter of the financial year ending with the date specified in column (2) of the Table below by the due date specified in the corresponding entry in column (3) of the said Table:

| S. No. | Date of ending of the quarter of financial year | Due date of the financial year |
|--------|---|--------------------------------|
| 1 | 30th June | 7th July |
| 2 | 30th September | 7th October |
| 3 | 31st December | 7th January |
| 4 | 31st March | 31st March |

Furnishing of statement [Section 167]

| | | |
|-----|---|--|
| 167 | Furnishing the statement | Every assessee or e-commerce operator shall, within the time prescribed after the end of the FY, submit a statement in the prescribed Form # 1, on or by 30th June immediately following the FY, setting forth all details for specified services pertaining to that FY |
| | Revised Statement | If the assessee or e-commerce operator notices omissions / errors / wrong details, he can furnish a revised statement before the expiry of 2 years from the end of the FY in which the specified service was provided. |
| | Notice by the Assessing Officer (A.O.) | Where any assessee or e-commerce operator has failed to file the statement within the prescribed time, the A.O. is empowered to issue a notice calling for the statement and in which case the statement has to be furnished within 30 days of date of serving of such notice. |
| 168 | Processing of the Statement | The statement shall be processed, and the amount payable along with interest if any, shall be computed towards the Equalization Levy. The net amount payable by or refundable to the assessee or e-commerce operator has to be worked out and an intimation must be served upon the assessee. However, no intimation is to be sent after the expiry of one year, from the end of the FY in which the statement is furnished. |
| 169 | Rectification of mistake | With a view to rectifying a mistake apparent on the record, the A.O. may amend the intimation and such intimation must be amended within one year from the end of the FY in which the intimation sought to be amended was issued. |
| 170 | Interest on delayed payments | Every assessee or e-commerce operator who fails to deposit to the credit of the Central Government, the applicable Equalization Levy, within 7th of the month following the month in which it was deducted, the assessee shall be liable to pay Interest @ 1% of such levy for every month / part of the month of delay. |
| 171 | Penalty | If the assessee or e-commerce operator fails to deduct the Equalization Levy, in addition to the Equalization Levy and Interest, penalty equal to the amount of Equalization Levy that he failed to deduct would be applicable. If the assessee fails to remit the Equalization Levy so deducted to the credit of the Government by 7th of the following month, a penalty of INR 1000 per day would be leviable, subject to a maximum of the equalization levy that he was to deduct. |
| 172 | Penalty for delay in furnishing the statement | If the assessee fails to furnish the statement within 30th June of the following FY, or within 30 days of the notice served by the A.O., a penalty of INR 100 per day is leviable on the assessee. |

An assessee aggrieved by an order of the A.O., may appeal to the Commissioner of Income Tax (Appeals) within 30 days of receipt of date of order. An assessee aggrieved by an order of the Commissioner, may appeal to the Appellate Tribunal within 60 days of receipt of date of order.

Illustration 6:

DEF Ltd. is in the business of manufacture and sale of formal apparels and in order to expand its footprints globally, has launched a massive online campaign. For the purpose of the online advertisements, it utilized the services of GHI Ltd., based out of Singapore. During the PY, DEF Ltd. paid a consideration of INR 20,00,000 to GHI Ltd. for such services.

Entail the implications if:

- (a) GHI Ltd. has no permanent establishment in India.
- (b) GHI Ltd. has a permanent establishment in India.

Solution:

- (a) In case GHI Ltd. has no permanent establishment in India, the consideration paid to GHI Ltd. by DEF Ltd. would attract Equalization Levy to be deducted @ 6%. Hence, INR 120,000 has to be deducted by DEF Ltd. and deposited to the credit of the Central Government within 7th of the following month. Non- deduction of equalization levy would attract a disallowance u/s 40(a)(ib) of 100% of the amount paid, while computing business income.
- (b) In case GHI Ltd. has a permanent establishment in India, Equalization Levy would not be attracted.

Therefore DEF Ltd. need not deduct Equalization Levy from the payment of consideration to GHI Ltd. However, tax has to be deducted u/s 195 in respect of such payments towards TDS. Non-deduction of TDS would attract a disallowance u/s 40(a)(i) of 100% of the amount paid, while computing business income.

CASE 1

Mr. DP has advertised on Facebook for his business purpose. For that, he has to pay Rs. 2,00,000 to Facebook for said advertising services. Discuss the tax implications under chapter VIII read with Section 10(50) of Income Tax Act, 1961.

Solution:

Mr. DP deduct Equalization Levy = 6% of 2,00,000 =Rs. 12,000 and Pay balance Rs. 1,88,000 to Facebook, the said advertisement. As per section 10(50) of the Income tax Act, 1961, Rs. 2,00,000 shall be exempted in the hands of Facebook.

CASE 2

Mama web online portal owned by Kremal corp. (US Based Company) providing online platform to Indian and foreign customers. Goods and services provided to Indian customer's amounts to Rs. 20 crores were provided to Non-resident amounting to Rs. 70 crores (other than u/s 165 & 165A). However, online services provided to Indian Customer XL Virtual by way of online advertisement amounts to Rs. 10,00,000. Discus the tax implications in relation to Equalization Levy?

Solution:

1. If Mama web online portal has PE in India. In above case, Equalization Levy is not applicable and company is required to pay tax as per normal income tax provisions.
2. If Mama web online portal does not have PE in India. In above case, Equalization Levy is applicable.
 - EL payable by Mama Web online portal to Govt. =2% *20 Crores = Rs. 4,00,000
 - XL Virtual is required to deduct Equalization Levy for online advertisement = 6% of 10,00,000 = Rs. 60,000

CASE 3

Nozy Inc., a USA based company, is carrying on the business of manufacture and sale of Cosmetic". In order to increase its Indian Market share, Company launched a massive advertisement campaign of its products. For the purpose of online advertisement, it utilized the services of Kuka Inc., a Ghana based company which also owns and operates a digital platform. The gross receipt of Kuka Inc from provision of such services during the P.Y. 2025-26 is Rs 3 crores. During the previous year 2025-26, Nozy Inc. paid Rs. 5 lakhs to Kuka Inc. for such services. Discuss the tax implications in line with reference to Equalization Levy If –

- (a) Nozy Inc. and Kuka Inc. have no PE in India
- (b) Nozy Inc. has a PE in India but Kuka Inc. has not PE in India
- (c) Kuka Inc. has a PE in India and the advertisement services are effectively connected with such PE

Solution:**(1) Nozy Inc. and Kuka Inc. have no PE in India**

- Equalization levy would not be applicable. Therefore, the Nozy Inc. is not required to deduct equalization levy @ 6%
- Equalization levy @2% under section 165A is leviable on Rs. 5 lakhs as the amount of consideration received by Kuka Inc, an e-commerce operator from e-commerce services provided by it to Nozy Inc., a non-resident in the specified circumstance (i.e. sale of advertisement) which targets a customer, who is resident in India, since the gross receipt of Kuka Inc. in the P.Y. 2025-26 exceeds Rs. 2 crores.

(2) Nozy Inc. has a PE in India but Kuka Inc. has not

- Equalization levy @6% is leviable on Rs 5,00,000 received by Kuka Inc., a non-resident not having a PE in India.
- Hence, Nozy Inc. is required to deduct equalisation levy of Rs 30,000 (6% * 5 lakhs) as Services provided by Nozy Inc., a non-resident having no permanent establishment in India.
- Since, equalisation levy is attracted on the amount of Rs 5 lakhs, the said amount is exempt from income-tax by virtue of section 10(50) of the Income-tax Act, 1961.

(3) Kuka Inc. has a PE in India and the advertisement services are connected with such PE

- Equalisation levy would not be applicable as the non-resident service provider Kuka Inc., has a PE in India and the service is effectively connected to the permanent establishment in India.
- Hence, Nozy Inc. is not required to deduct equalisation levy on Rs 5 lakhs, being the amount paid towards online advertisement services to Kuka Inc, in this case.
- Since equalisation levy is not applicable in this case hence no exemption under section 10(50) of the Income-tax Act, 1961 would be available.

ASPECTS OF AMALGAMATIONS, MERGERS AND DEMERGERS

The Indian Income Tax Act, 1961 ("ITA") contains several provisions that deal with the taxation of certain specific transactions. In the Indian context, M&A can be structured in different ways and the tax implications vary based on the structure that has been adopted for a particular acquisition. The methods in which an acquisition can be undertaken are:

1. Slump Sale: A slump sale is a sale of a business/ undertaking by a seller as a going concern to an acquirer, without specific values being assigned to individual assets;

2. Merger: This entails a court approved process whereby one or more companies merge with another company or two or more companies merge together to form one company;
3. Demerger: This entails a court approved process whereby the business / undertaking of one company is demerged into a resulting company;
4. Share Purchase: This envisages the purchase of the shares of the target company by an acquirer;
5. Asset Sale: An asset sale is another method of transfer of business, whereby individual assets / liabilities are cherry picked by an acquirer.

Section 2(1B) of the Income Tax Act defines the term “Amalgamation” as

“**amalgamation**”, in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that:

- (i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;
- (ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;
- (iii) shareholders holding not less than three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation,

other-wise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first-mentioned company;

(Example: Say, X Ltd merges with Y Ltd in a scheme of amalgamation and immediately before the amalgamation, Y Ltd held 20% of shares in X Ltd, the above mentioned condition will be satisfied if shareholders holding not less than 75% in the value of remaining 80% of shares in X Ltd i.e. 60% thereof, become shareholders in Y Ltd by virtue of amalgamation) otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first mentioned company.

Section 2(19AA) of the Income Tax Act defines the term “Demerger” as

“**demerger**”, in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956 (1 of 1956), by a demerged company of its one or more undertakings to any resulting company in such a manner that:

- (i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;
- (ii) all the liabilities relating to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;
- (iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger:

Provided that the provisions of this sub-clause shall not apply where the resulting company records the value of the property and the liabilities of the undertaking or undertakings at a value different from the

value appearing in the books of account of the demerged company, immediately before the demerger, in compliance to the Indian Accounting Standards specified in Annexure to the Companies (Indian Accounting Standards) Rules, 2015;

- (iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis except where the resulting company itself is a shareholder of the demerged company;
- (v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;
- (vi) the transfer of the undertaking is on a going concern basis;
- (vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of Sec. 72A by the Central Government in this behalf.

Explanation 1: For the purposes of this clause, “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 2: For the purposes of this clause, the liabilities referred to in sub-clause (ii), shall include-

- a) the liabilities which arise out of the activities or operations of the undertaking;
- b) the specific loans or borrowings (including debentures) raised, incurred and utilised solely for the activities or operations of the undertaking; and
- c) in cases, other than those referred to in clause (a) or clause (b), so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger

Explanation 3: For determining the value of the property referred to in sub-clause (iii), any change in the value of assets consequent to their revaluation shall be ignored.

Explanation 4: For the purposes of this clause, the splitting up or the reconstruction of any authority or a body constituted or established under a Central, State or Provincial Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies, as the case may be, shall be deemed to be a demerger if such split up or reconstruction fulfils such conditions as may be notified in the Official Gazette, by the Central Government.

Explanation 5: For the purposes of this clause, the reconstruction or splitting up of a company, which ceased to be a public sector company as a result of transfer of its shares by the Central Government, into separate companies, shall be deemed to be a demerger, if such reconstruction or splitting up has been made to give effect to any condition attached to the said transfer of shares and also fulfils such other conditions as may be notified by the Central Government in the Official Gazette.

Explanation 6: For the purposes of this clause, the reconstruction or splitting up of a public sector company into separate companies shall be deemed to be a demerger, if such reconstruction or splitting up has been made to transfer any asset of the demerged company to the resulting company and the resulting company-

- i. is a public sector company on the appointed day indicated in such scheme, as may be approved by the Central Government or any other body authorised under the provisions of the Companies Act, 2013

(18 of 2013) or any other law for the time being in force governing such public sector companies in this behalf; and

- ii. fulfils such other conditions as may be notified by the Central Government in the Official Gazette in this behalf;

(19AAA) “demerged company” means the company whose undertaking is transferred, pursuant to a demerger, to a resulting company;

Capital Gains

Under Section 47(vi) and (vii) transfer does not include any transfer in a scheme of amalgamation of a capital asset by the amalgamating company to the amalgamated company if the latter is an Indian company. From the assessment year 1993-94, any transfer of shares in an Indian company held by a foreign company to another foreign company in pursuance of a scheme of amalgamation between the two foreign companies will not be regarded as a transfer for the purpose of levying tax on capital gains. This provision will apply if $\geq 25\%$ of the shareholders of the amalgamating company continue to remain shareholders of the amalgamated foreign company and such transfer does not attract tax in the country in which the amalgamating company is situated.

Further, the term “transfer” does not include any transfer by a shareholder in a scheme of amalgamation, of a capital asset, being shares held by him in the amalgamating company, if the transfer is made in consideration of allotment to him, shares in the amalgamated company, and the amalgamated company is an Indian Company. Even, per se, amalgamation doesn't entail exchange or relinquishment of assets, and hence, capital gains tax is not attracted. The same was upheld in the case CIT vs. Rasik Lal Manek. However, the benefit doesn't continue if the shareholders of amalgamating company are allotted something more than the share in the amalgamated company, viz., bonds / debentures etc. as this was upheld in the case of CIT vs. Gautam Sarabhai Trust.

| Tax Treatment | | |
|--|--|---|
| Shareholders | Amalgamating Company | Amalgamated Company |
| According to Section 47, It is not considered to be “Transfer” hence, no capital gain would be attracted when shares are allotted to shareholders of amalgamating company. | According to Section 47, No capital gain will be attracted on transfer of capital assets by amalgamating company to amalgamated company. | As per section 49(1), Cost of Acquisition of the assets becomes the property of the amalgamated company. PGBP losses and unabsorbed depreciation of amalgamating company can be carried forward and set off by amalgamated company. |

Carry Forward and Set Off of Accumulated loss and unabsorbed depreciation of the amalgamating company [Section 72A]

A special provision is made which relaxes the provision relating to carrying forward and set off of accumulated business loss and unabsorbed depreciation allowance in certain cases of amalgamation. Where there has been an amalgamation of:

- (i) a company owning an industrial undertaking or a ship or a hotel with another company, or
- (ii) an amalgamation of a banking company with a specified bank,
- (iii) 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.

then the accumulated losses or the unabsorbed depreciation of the amalgamating company shall be deemed

to be the loss or the unabsorbed depreciation of the amalgamated company for the PY in which the transfer was effected. Consequently, the amalgamated company can carry forward such loss for 8 AY's immediately succeeding the relevant AY in which the amalgamation was effected.

However, the above relaxations shall not be allowed if:

- (a) the amalgamated company is engaged in the business in which the accumulated loss or depreciation remains unabsorbed for ≥ 3 years;
- (b) the amalgamated company has held continuously as on date of the amalgamation $\geq 3/4$ ths of the book value of fixed assets 2 years prior to the date of amalgamation;
- (c) the amalgamated company holds continuously for ≥ 5 years from the date of amalgamation, $\geq 3/4$ ths of the book value of fixed assets of the amalgamating company so acquired;
- (d) the amalgamated company continues the business of the amalgamating company for ≥ 5 years from the date of amalgamation.

If any of the above conditions are not complied with, then the set off of loss / depreciation, made in any PY, in the hands of the amalgamated company, shall be deemed to be the income of the amalgamated company chargeable to tax for the year of non-compliance.

| Treatment of Expenditure | |
|--|---|
| Preliminary Expenses | <p>The benefit of amortization of preliminary expenses under section 35D are ordinarily available only to the assessee who incurred the expenditure. However, the benefit will not be lost in case the undertaking of an Indian company which is entitled to the amortization is transferred to another Indian company in a scheme of amalgamation within the 10 years/ 5-year period of amortization.</p> <p>In that event, the deduction in respect of previous year in which the amalgamation takes place and the following previous year within the 10 years / 5 years period will be allowed to the amalgamated company and not to the amalgamating company.</p> |
| Capital Expenditure on Scientific Research & Know-how | <p>In case of an amalgamation, if the amalgamating company transfers to the amalgamated company, which is an Indian company, any asset representing capital expenditure on scientific research, provision of section 35 would apply to the amalgamated company as they would have applied to amalgamating company if the latter had not transferred the asset. The same principle applies in essence for the expenditure on know-how.</p> |
| Expenditure on Amalgamation | <p>Section 35DD provides that where an assessee being an Indian company, incurs any expenditure, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee shall be allowed, a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the PY in which such amalgamation / demerger takes place.</p> |

Students may refer to Lesson No. 7, titled "Taxation and stamp duty aspects of Corporate Restructuring" of paper 6 "Corporate Restructuring, Valuation & Insolvency" under professional programme for aspects relating to taxation of Corporate Restructuring

LESSON ROUNDUP

- Dividend income are taxable under the head 'Income from other sources' irrespective of fact that person held securities either as a trader or as an investor.
- Assessee can claim a deduction of interest expenses for earning a dividend income (other than any payment by a company on purchase of its own shares from a shareholder i.e. buy-back of shares) and Interest on money borrowed for investing in the shares can be claimed as a deduction subject to a maximum of 20% of dividends or income in respect of units of a mutual fund
- **“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.
- Any profits or gains arising from the slump sale effected in the previous year shall be chargeable to income-tax as capital gains.
- **“Buy-back”** means purchase by a company of its own shares in accordance with the provisions of any law for the time being in force relating to companies.
- Any amount of distributed income by the company on buy-back of shares in the hands of a shareholder.
- **“Carbon Credit”** in respect of one unit shall mean reduction of one tonne of carbon dioxide emissions or emissions of its equivalent gases which is validated by the United Nations Framework on Climate Change and which can be traded in market at its prevailing market price.
- **Merger:** This entails a court approved process whereby one or more companies merge with another company or two or more companies merge together to form one company;
- **Demerger:** This entails a court approved process whereby the business / undertaking of one company is demerged into a resulting company;
- **Share Purchase:** This envisages the purchase of the shares of the target company by an acquirer;
- **Asset Sale:** An asset sale is another method of transfer of business, whereby individual assets / liabilities are cherry picked by an acquirer.

TEST YOURSELF

These are meant for recapitulation only. Answer to the questions are not to be submitted for evaluation.

1. X Limited has transferred its unit C to Y Ltd. by way of slump sale on November 30, 2025. The balance sheet of X Ltd. as on that date is given below:

| Liabilities | (in Lakh) | Assets | (in Lakh) |
|---------------------|-----------|--------------|-----------|
| Paid up Capital | 1700 | Fixed Assets | |
| Reserve and Surplus | 620 | Unit A | 150 |
| Liabilities: | | Unit B | 150 |
| Unit A | 40 | Unit C | 550 |
| Unit B | 110 | Other Assets | |
| Unit C | 90 | Unit A | 520 |
| | | Unit B | 800 |
| | | Unit C | 390 |
| Total | 2560 | Total | 2560 |

Compute the capital gains arising from slump sale of unit C and tax on such capital gains with the help of the following information.

- Lumpsum consideration on transfer of unit C – Rs. 880 Lakhs

- Fixed assets of Units C include land which was purchased at Rs. 60 lakhs in August 2022 and revalued at Rs. 90 lakhs on March 31, 2025.
- Other fixed assets are reflected at Rs. 460 lakhs (i.e. 550 lakhs less value of land) which represent written down value of those assets as per books. The written down value of these assets u/s 43(6) of the Act is Rs. 410 lakhs.
- Unit C was set up by X ltd in July, 2006.

ELABORATIVE QUESTIONS

1. Discuss the tax implication in case Dividend Income?
2. Whether interest expenses incurred can be claimed as deduction while computing dividend income? If Yes, upto what limit? Explain the provision in details with examples.
3. What is slump sale? Explain the provisions related to computation of capital gains in case of slump sale transactions.
4. What are the points / criteria to fall the transaction under slump sale?
5. What is buy back of shares? What is the tax implication in case of buy back of shares?
6. Explain the provisions related to tax on distributed income of domestic company for buy back of shares
7. Discuss the reduction of share capital and its tax implication?
8. What is inter-corporate dividend? Explain the provision in brief along with examples?
9. What is Amalgamation? Explain the provision related to tax implication in case of Amalgamation as well as the provision related to carried forward and set-off of losses in case of Amalgamation

LIST OF FURTHER READINGS

- **Direct Taxes Law and Practice**
Author: Dr. Vinod K. Singhanian & Dr. Kapil Singhanian
Publisher: Taxmann
- **Direct Taxes Ready Reckoner with Tax Planning**
Author: Dr. Girish Ahuja & Dr. Ravi Gupta
Publisher: Wolters Kluwer

OTHER REFERENCES (INCLUDING WEBSITES AND VIDEO LINKS)

- **Income Tax Act, 1961:** <https://www.incometaxindia.gov.in/Pages/acts/income-tax-act.aspx>
- **Income Tax Rules, 1962:** <https://www.incometaxindia.gov.in/Pages/rules/income-tax-rules-1962.aspx>
- **Circulars:** <https://www.incometaxindia.gov.in/Pages/communications/circulars.aspx>
- **Notifications:** <https://www.incometaxindia.gov.in/Pages/communications/notifications.aspx>