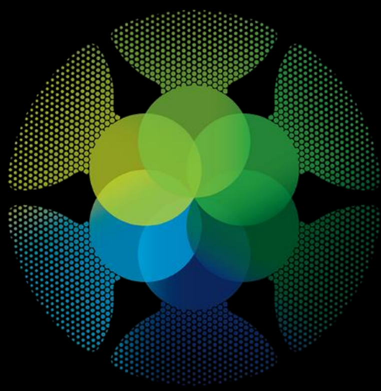
Deloitte.

India | Tax & Regulatory | For private circulation only | 12 September 2018



Mergers and Acquisition Alert
Delivering Clarity

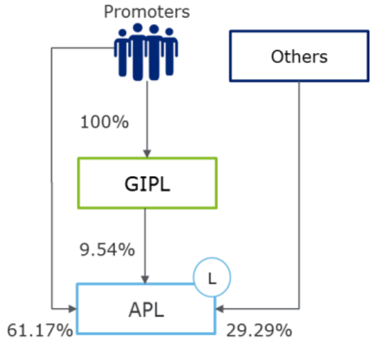
Income tax authorities invoke GAAR provisions while responding to NCLT Mumbai, resulting in rejection of scheme of amalgamation and arrangement

Issue no: M&A/06/2018

In this issue:

Facts of the case

- A scheme of amalgamation and arrangement (Scheme) was filed before National Company Law Tribunal, Mumbai (NCLT) proposing the following:
  - Merger of Gabs Investments Private Limited (GIPL) with Ajanta Pharma Limited (APL);
  - Reduction of share capital held by GIPL in APL;
  - GIPL held 8,392,262 shares of APL. In consideration, APL to issue 8,392,262 equity shares to promoters;
  - APL is a listed company;
  - GIPL had no other businesses other than investments in APL.
- Group structure is as below:



- The rationale behind the Scheme was to simplify the group structure and reduce the shareholding tiers such that promoters are directly able to hold shares in APL.
- No adverse comments were reported in the independent valuer's report, merchant banker's fairness opinion and in the observation letter from SEBI dated 19 July 2017.
- Income tax authorities (ITA) had raised objections on the Scheme. Invoking provisions of GAAR, the ITA argued that the Scheme was an Impermissible Avoidance Arrangement resulting in a deliberate measure to avoid taxes.
- The ITA contended that there would be revenue loss of INR 421.7 Crores on the following basis:
  - The ITA assumed the shares would be sold in the open market and the company would distribute profit on the sale of shares.
  - The ITA arrived at an income of INR 958.3 Crores (excess of market price of INR 1007.1 Crores over cost of INR 48.7 Crores).
  - The ITA considered the income as business income as GIPL was an investment company. The ITA proposed to levy tax at the rate of 30 per cent, amounting to INR 287.5 Crores.
  - The ITA computed a dividend distribution tax (DDT) of INR 134.2 Crores on post-tax profits.
- Petitioner companies had represented to the NCLT stating various judgements/ orders with respect to sanctioning of schemes with similar objectives.

Ruling of NCLT

- The NCLT opined as follows:
  - With investment of INR 48.7 Crores, promoters would get shares worth INR 1,477 Crores (market value as on 31.3.2017) without payment of income tax.
  - Through this Scheme, GIPL and promoters were avoiding tax liability.
  - The Scheme would benefit only promoters and no public interest is envisaged to be served.
- The NCLT relied on the judgement of National Company Law Appellate Tribunal (NCLAT) in the matter of Wiki Kids Ltd v/s Aventel Ltd (AT NO 285 of 2017) wherein NCLAT held that if the scheme was not in public interest the same can be rejected by NCLT.

Conclusion

This is the first merger scheme where the ITA has invoked provisions of GAAR. It shows that the ITA will look at the objectives and the outcome of the Scheme to determine whether the Scheme was prepared with the primary purpose of avoidance of tax. Tax payers would have to ensure that there are sufficient commercial reasons for any scheme of amalgamation or arrangement.

Source:

- NCLT Mumbai Bench order delivered on 05 September 2018 in the scheme of amalgamation and arrangement between Gabs Investments Private Limited and Ajanta Pharma Limited and their respective shareholders – CSP No. 995 of 2017 and CSP No. 996 of 2017 in CSA No. 791 and 792 of 2017
- Public documents as available on https://www.bseindia.com

Do you know about Dbriefs?

Dbriefs are live webcasts that give valuable insights on important developments affecting your business. To register, visit the Dbriefs page.

Download the report

Deloitte makes an impact that matters