



## **Regulatory Alert** Delivering Clarity

### **SEBI clarifies on applicability of SAST Regulations upon conversion of company into LLP**

**Issue no:** RA/18/2018

**In this issue:**

[Synopsis](#)  
[Facts](#)  
[Question of law](#)  
[Tax and Regulatory implications](#)  
[Informal guidance of SEBI](#)  
[Conclusion](#)  
[Deloitte tax@hand App](#)  
[Do you know about Dbriefs?](#)

## Synopsis

The Securities and Exchange Board of India (SEBI), by way of an informal guidance, clarified that acquisition/ transfer of shares in Target Company pursuant to conversion of existing shareholder and promoter (Acquirer), from private limited company into LLP, would fall within the meaning of 'succession' under SAST Regulations and would qualify for exemption from making an open offer. The exemption from making an open offer is subject to the shareholding of the LLP being the same as that of Acquirer in the Target Company, with no change in control.

## Facts

- Fidelo Foods Private Limited (FFPL) is the existing shareholder and promoter of India Finsec Limited (Target Company), holding 18.19 per cent shares in the Target Company. The shares of the target company are listed on the BSE.
- FFPL proposed to change its status from private limited company to a Limited Liability Partnership (LLP) pursuant to which the shareholding of FFPL shall be transferred to/ or be acquired by the LLP.
- There would be no change in the controlling interest of the Target Company.

## Question of law

The question that arose before SEBI is whether such transfer/acquisition upon conversion of a company into LLP, would trigger open offer obligations under Regulation 3 of SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011 (SAST Regulations).

## Tax and Regulatory Implications

- In accordance with Regulation 3(1) of SAST Regulations, acquisition of/transfer of shares would trigger an open offer obligation, if it entitles the Acquirer along with the person acting in concert, to exercise 25% or more voting right in the Target Company.
- However, Regulation 10(1)(g) of SAST Regulations states that the acquisition of shares by way of succession, transmission or inheritance is exempt from the obligation to make an open offer under Regulations 3 and 4 of SAST.
- Section 47(xiiib) of the Income-tax Act, 1961 (the IT Act) provides the conditions that need to be satisfied in order for conversion of a private company/ unlisted public company into a LLP, and being exempt from capital gains tax in the hands of

both the company as well as the shareholders. While Section 47(xiiib) imposes certain restrictions on post conversion transactions - such as restrictions on distribution of accumulated profits and change in profit sharing ratio - the conditions of allowing only a company having total turnover etc., up to INR 6 million and total assets up to INR 50 million in all the three years prior to the conversion, being eligible for the above exemption are the most burdensome. The above restrictions have impaired the ability of promoter holding companies to move into a more efficient model of a LLP. While a conversion into a LLP without complying with the conditions of Section 47(xiiib) could be explored, achieving tax neutrality (especially on the shareholders' side) based on general principles may be a long-winded and litigative proposition.

## **Informal guidance of SEBI**

- It was stated that the acquisition/transfer of shares in Target Company is pursuant to conversion of a private limited company into a LLP and the ownership of business of FFPL was proposed to be transferred to the LLP without any change in the nature of business and control.
- SEBI clarified that the proposed conversion would fall within the meaning of 'succession' under regulation 10(1)(g) of the SAST Regulations and would qualify for an exemption from making an open offer, subject to the shareholding of the LLP being the same as that of FFPL in the Target Company, with no change in control.
- SEBI further stated that upon conversion, the LLP would form part of the promoter group and therefore, LLP and the Target Company would be under an obligation to make necessary disclosures under the SAST Regulations, SEBI (Prohibition of Insider Trading) Regulations, 2015 and any other law wherever applicable.
- Such exemption would be applicable subject to compliance of conditions prescribed in regulation 10 of the SAST Regulations.

## **Conclusion**

The SEBI informal guidance, though case and fact-specific, is important from the perspective of corporate restructuring. The guidance lays down the conditions for seeking an exemption from obligation to make an open offer on conversion of promoter entity organized as a company, into a LLP. However, different facts or conditions might lead to a different view/conclusion from SEBI.

**Source:** Informal Guidance issued by SEBI dated July 23, 2018 viz no. CFD/DCR2/OW/P/2018/20660/1 seeking clarification on the requirement of open offer obligations under regulation 3 in case of conversion of the acquirer /promoter from private limited company into LLP.

## Deloitte tax@hand App

**Current. Comprehensive. Convenient.**

Download [tax@hand](#) app, a secure digital platform for timely global and regional news, perspectives, and resources. Do visit the tax@hand webpage [here](#).



**Deloitte.**

**IOS**



Download from App Store

**Android**



Download from Google Play

**Website**



Add to favorites

## 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

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. Please see [www.deloitte.com/about](http://www.deloitte.com/about) for a more detailed description of DTTL and its member firms.

This material and the information contained herein prepared by Deloitte Touche Tohmatsu India LLP (DTTI LLP) is intended to provide general information on a particular subject or subjects and is not an exhaustive treatment of such subject(s). This material contains information sourced from third party sites (external sites).

DTTI LLP is not responsible for any loss whatsoever caused due to reliance placed on information sourced from such external sites. None of DTTI LLP, Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network") is, by means of this material, rendering professional advice or services. This information is not intended to be relied upon as the sole basis for any decision which may affect you or your business. Before making any decision or taking any action that might affect your personal finances or business, you should consult a qualified professional adviser.

No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this material.

©2018 Deloitte Touche Tohmatsu India LLP. Member of Deloitte Touche Tohmatsu Limited