

TAX FLASH NEWS

The scheme of amalgamation has been approved based on, inter alia, an undertaking given by a company that in the event of any demand by the tax department, transferee company would discharge the liability

Background

A scheme of amalgamation was filed before the Punjab and Haryana High Court (High Court) in the case of Ludhiana Holdings Ltd.¹ (the taxpayer company). The tax department had contended that some of the assets have not been included in the books of the transferor company and action is required on those assets. Further the share exchange ratio does not appear to be in the best interest of the shareholders, creditors, employees, customers of the transferee company. Therefore, the scheme should not be approved.

The High Court rejected the tax department's contentions and approved the scheme of amalgamation based on views of the regional director and the official liquidator, the resolutions passed by the board of directors, the consents given by the shareholders of the transferor company, the unanimous approval of the scheme by shareholders and creditors of the transferee company, etc. The High Court also relied on an undertaking given by the authorised signatory of the transferor company that in the eventuality of the tax department raising any demand regarding statutory dues payable to the department, the same shall be discharged by the transferee company in accordance with law.

Facts of the case

- The taxpayer company (transferor company) and Oswal Woollen Mills Ltd. (transferee company) have filed the petition under Sections 391 to 394 of the Companies Act, 1956, for sanctioning a scheme of amalgamation by virtue of which it is proposed to amalgamate the transferor company with the transferee company.

- As per the order passed in the company petition, secured and unsecured creditors of the transferor company were directed to be dispensed with in view of the consents received from the eight equity shareholders of the transferor company and in view of the fact that the transferor company does not have any creditors, secured or unsecured.
- The official liquidator has also filed his report along with the report of the chartered accountant appointed for scrutinising the books of account and papers of the transferor company.

Tax department's contentions

- It appears that the tax department was of the view that there may be some assets, which have not been included in the books of the transferor company and action is required on those assets.
- The share exchange ratio does not appear to be in the best interest of the shareholders, creditors, employees, customers of the transferee company.

Taxpayer's contentions

- The taxpayer contended that the observation made by the tax department is vague and ambiguous. Further, the current balance sheet and assets submitted to this Court and the scheme clearly prescribes that the entire assets of the transferor company stands transferred to the transferee company.

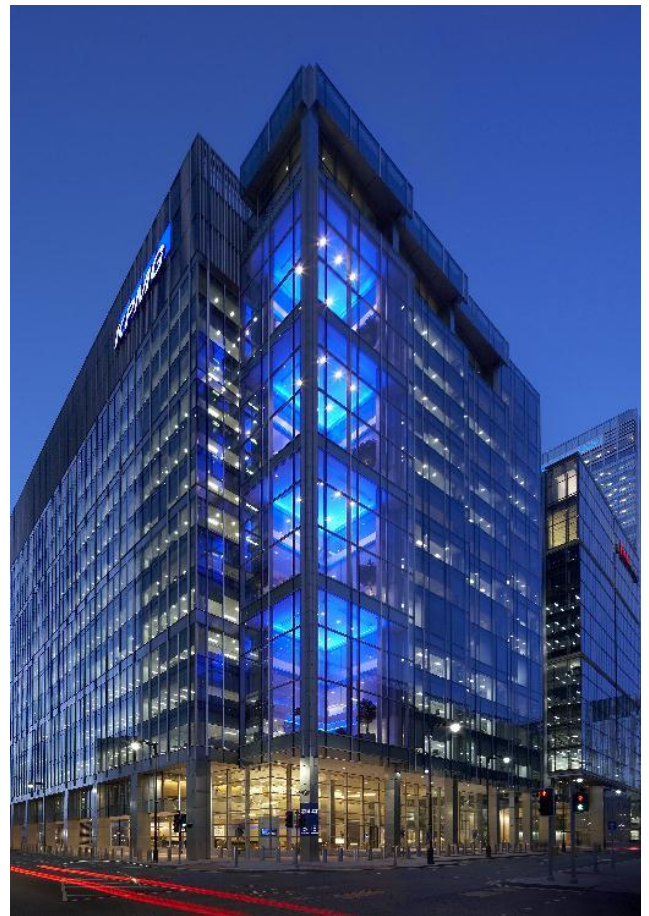
¹ Ludhiana Holdings Ltd., In re [2015] 57 taxmann.com 301 (P&H)

- Since an undertaking has been given by the authorised signatory of the company that in the event of any demand raised by the tax department, the transferee company shall duly discharge the same, in accordance with law; the observation of the tax department is irrelevant and meaningless.
- Valuation of the assets and liabilities of companies is done by an independent expert to ensure the fairness of the transaction. Before formulating the proposed scheme of amalgamation, expert opinion was obtained by both companies from a firm of chartered accountants who have considered all the relevant aspects and suggested the exchange ratio keeping in view the valuation of shares of respective companies.
- The shareholders of both the companies have approved the scheme, which necessarily includes the share exchange ratio. The shareholders are the sole authority to decide the exchange ratio of merger and once the shareholders have approved and accepted the same it would not lie with the tax department to sit in the judgment on the wisdom and decision of the shareholders.
- The official liquidator in his report submitted that the amalgamation is not prejudicial to the interest of its members or public. Thus the objections/observations made by the tax department are unsustainable and irrelevant.

- Accordingly, the scheme of amalgamation has been sanctioned.

Our comments

This is a welcome ruling where the High Court approved the scheme of amalgamation based on, *inter alia*, an undertaking given by the company stating that in the eventuality of the tax department raising any demand regarding statutory dues payable to the department, the same shall be discharged by the transferee company in accordance with the law.



High Court's ruling

- On perusal of the scheme of amalgamation and taking into consideration the views of the regional director and the official liquidator, the resolutions passed by the board of directors, the consents given by the shareholders of the transferor company, the unanimous approval of the scheme by the shareholders, secured creditors and unsecured creditors of the transferee company and the submissions made by the taxpayer, there is no reason to decline the approval/sanction of the scheme of amalgamation to amalgamate and merge the transferor company with the transferee company. Accordingly, the objections/observations made by the tax department were overruled.
- The tax department's observations have been suitably covered because all liabilities of the transferor company are being transferred to the transferee company, and the undertaking given by the authorised signatory of the transferor company that in the eventuality of the tax department raising any demand regarding statutory dues payable to the department, the same shall be discharged by the transferee company in accordance with law.

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