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Slump Sale - Effect of Amendments by Finance Act 2021

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Finance Act 2021 has made certain important amendments to Income Tax Act (the Act) in respect of provisions relating to taxation of capital gains arising on Slump Sale. These are discussed below:

1. Amendment in Section 2(42C) relating to definition of Slump Sale:

The existing provisions in Section 2(42C) of the Act prior to the amendment by Finance Act 2021, defined 'Slump Sale' as -

'The transfer of one or more undertaking, as a result of sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales'.

The amended definition of 'Slump Sale' now reads as under -

"The transfer of one or more [undertaking, by any means,] for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales".

Further, a new Explanation has been inserted in Section 2(42C) providing that, *'For the purposes of this clause, "transfer" shall have the meaning assigned to it in clause (47)'* of Section 2.

These amendments widen the scope of 'Slump Sale' to include all types of transfers that fulfil other conditions of Section 2(42C).

These overrule decisions of Hon'ble Bombay HC in *Bharat Bijlee Ltd'* and of Madras High court in *Areva T&D India Ltd.*², wherein the Courts had held that the definition of 'Slump Sale' under Section 2(42C) is restricted to transfer resulting from 'sale' and does not include transfer by other modes of transfers mentioned Section 2(47) of the Act, such as exchange for non-monetary considerations.

2. Amendment in Section 50B relating to computation of Capital Gains:

Section 50B (2) of the Act provides the method for computing capital gains in the case of Slump Sale of an undertaking. Prior to the amendment by Finance Act 2021 it provided that for computing capital gains resulting on Slump Sale of an undertaking the 'Net Worth' of the undertaking shall be deemed to be its

¹ [2014] 224 Taxman 282 (Bom)

¹ [2021] 434 ITR 604 (Madras)

cost of acquisition, without allowing any cost indexation. In turn Explanations 1 and 2 below Section 50B (2) provided the method for computing the 'Net Worth' of the undertaking.

Thus, under the existing provisions the difference between the transfer consideration as agreed by the parties and the 'Net Worth' of the undertaking as computed under Explanations 1 and 2 below Section 50B, was treated as capital gain on slump sale.

Finance Act 2021 has made two changes in Section 50B in this respect, by substituting a new clause in place of the existing clause (2) of this Section:

- One, it has provided that for computing 'Net Worth' of the undertaking value of 'goodwill' of the undertaking will be taken as Nil, unless the 'goodwill' was acquired by the transferor from a previous owner.
- Two, it has provided that for computing Capital Gains, the Fair Market Value (FMV) of the undertaking, computed as per prescribed procedure, shall be deemed to be the transfer consideration instead of the amount agreed by the parties to the transaction.

CBDT has since notified Rule 11UAE laying down the methodology for computation of the FMV of an undertaking for the purposes of Section 50B of the Act.

3. Rule 11UAE - Computation of Fair Market Value for Section 50B

Rule 11UAE provides following two alternate formulas for computing FMV of the undertaking on the date of slump sale, and mandates that higher of the two values arrived at as per these methods will be taken as the FMV.

FMV-1 = A+B+C+D – L, where,

A= Book value of assets other than jewellery, artistic work, shares, securities and immovable property, income-tax paid, and any unamortised amount of deferred expenditure

B = Fair market value of jewellery and artistic work as per valuation report of a registered valuer

C = Fair market value of shares and securities as determined as per Rule 11UA

D = Stamp Duty value of the immovable property

L= Book value of liabilities excluding paid up share capital, Reserves and Surplus, and contingent liabilities.

FMV-2 = E+F+G+H, where,

E = Monetary consideration received or accruing on the transfer

F = Fair market value of non-monetary consideration received or accruing on the transfer represented by shares and securities as determined as per Rule 11UA

G = Price which the non-monetary consideration received or accruing as a result of the transfer represented by property, other than immovable property and shares and securities, would fetch if sold in the open market on the basis of the valuation report of a registered valuer

H = Stamp Duty value of the immovable property

4. Depreciation on 'goodwill' of Business or Profession:

Finance Act 2021 has also made following changes in the Act, the effect of which is that depreciation will henceforth not be admissible on 'goodwill' of business and profession:

- Definition of 'block of asset' in Section 2(11) has been amended to exclude 'goodwill of business or profession' from intangible assets.
- 'Goodwill of business or profession' has been removed from the definition of 'asset' in Section 32 of the Act.

These amendments will also have a bearing on the cases of Slump Sale.

As per existing practice in cases of Slump Sale of business undertaking as going concern, payment over and above book value of net tangible assets, was allocated by the buyer in its books of account as cost of acquisition of bundle of business and commercial rights, compendiously termed as 'goodwill'. Depreciation was admissible on these intangible assets. The practice had received judicial approval³.

Henceforth depreciation on 'goodwill' will not be admissible to the buyer in view of the above amendments. However, it needs to be noted that even after the above amendments, other intangible assets, being know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, remain eligible for depreciation. Accordingly, the buyer can undertake valuation exercise and documentation to attribute value to these types of intangible assets and claim depreciation on the same.

³ CIT v. Smiff Securities Ltd. (2012) 348 ITR 302 (SC); Triune Energy Services vs. DCIT (2016) 65 taxmann.com 288 (Delhi); Areva T&D India Ltd. v. Dy. CIT [2012] 208 Taxman 252 (Delhi)].