

Tax Wire



**Slump Sale consideration
to be determined based
on FMV for taxation**

- Rule 11UAE

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Background

Section 2(42C) of the Income-tax Act, 1961 (IT Act) defines '**slump sale**' as transfer of one or more undertakings for a lumpsum consideration without the value being assigned to individual assets and liabilities in such cases.

Section 2(19AA) defines '**undertaking**' as any part of an undertaking, or a unit/division of an undertaking or a business activity taken as a whole but does not include individual assets/liabilities/any combination thereof not constituting a business activity.

The computation mechanism of slump sale is provided in Section 50B of the IT Act. As per section 50B of the IT Act, the gains/(loss) arising from slump sale shall be taxed as Capital Gains/(loss). Depending upon the period of holding of the undertaking, the gain/(loss) could either be long-term or short-term.

Two amendments were made in the slump sale provisions by Finance Act 2021.

1. There was an ongoing debate on "Whether slump exchange will be considered as slump sale?" In order to clarify this, an amendment **to section 2(42C)** was made, where it has been clarified that **slump sale** means transfer of an **undertaking by any means and such transfer would cover all types of transfer as per section 2(47)** and not merely sale.
2. **Section 50B** was also amended to provide that the Fair Market Value (FMV) of the capital assets (being an undertaking or division transferred by way of slump sale) as on the date of transfer shall be deemed to be the

consideration and it shall be calculated in the manner to be prescribed.

The methodology for determining FMV of the capital Asset was to be prescribed by the Central Board of Direct Taxes (CBDT).

In this regard, recently CBDT has issued a notification¹ introducing a new Rule 11UAE in the Income-tax Rules, 1962 (IT Rules).

Computation Mechanism as per Rule 11UAE

For purpose of section 50B(2)(ii) of the IT Act, the FMV of capital assets shall be **higher** of following:

FMV1 as determined under Rule 11UAE(2) of IT Rules; or

FMV2 as determined under Rule 11UAE(3) of IT Rules

Formula for computing FMV1:

- **Jewellery, artistic work, shares** – Open market Price/ FMV of the Asset (as per section 11UA(1) of the IT rules or based on valuation report obtained from registered valuer²)
- **Immovable property** – Value adopted for the purpose of computing Stamp duty value (SDV) for such the property
- **Other assets** – Book value of the assets after adjusting income tax paid and amount which is shown as asset but does not represent the value of any asset.
- **Liabilities** – Book value of the liabilities excluding the following
 - I. Paid up equity share capital

¹ Notification No.68/2021/F.No.370142/16 /2021-TPL

² As defined in Rule 11U of the IT Rules

- II. Dividend amount on preference and equity shares set apart
- III. Reserves and surplus other than those set apart towards depreciation
- IV. Provision for taxation
- V. Provision for unascertained liabilities
- VI. Contingent liabilities other than arrears of dividends payable for cumulative preference shares

Formula for computing FMV2

FMV2 will be calculated as follows:

- **Monetary consideration** - received or accruing on transfer
- **Non-Monetary Consideration** –
 - I. **Immovable property** – SDV of the property
 - II. **Other Assets** - FMV/open market price of the Asset received (as per section 11UA(1) of the IT rules or based on valuation report obtained from registered valuer²)
 - III. For the purpose of determining FMV1 and FMV2, the valuation date shall be the slump sale date.

Advith Comments

While the Finance Act, 2021 has brought slump exchange amendment to tax from FY 2020-21, the Rules for computing the sale consideration is prescribed only now. The Notification does not specifically mention as to the date from which the Rule 11UAE shall be effective.

Hence, it is possible to contend that this Rule should be applicable only from the date of publication in the Official Gazette. Hence, in respect of slump sale concluded prior to the rule being notified, one could contend that there should not be any tax liability and to that extent the amendment is infructuous.

Further, the main concept of slump sale is sale of an undertaking for lumpsum consideration without assigning values to individual assets and liabilities. However, introduction of this rule is a deviation from such concept. These new rules are assigning values to individual assets to determine sale consideration in such transactions. This might result into the following questions/thoughts:

- Since this take away the real essence of the slump sales transaction, is it legally tenable?
- What more complication arise owing to such rule whereby the commercially agreed lump sale consideration are substituted with a rule based FMV determined on valuing each asset?
- Cases of genuine distress sale of undertaking at a going concern value which could be naturally lower than summation of individual value of each asset in the undertaking, would be considerably hit by these rules.
- Intra-group internal restructuring where the slump sale method was being used could now become extremely tax inefficient owing to these rules and taxpayers will have to evaluate such plans in light of these new rules.

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