

## GST implications in case of merger

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In today's world, mergers have become an indispensable element of corporate reorganization. GST is one of the major taxes which impact mergers. This article takes a look at the implications of GST provisions on mergers and also the procedure to be followed by the Transferor and the Transferee Companies. Let us assume a company ("the Transferor Company") merges into another company ("the Transferee Company"). All the assets and liabilities of the Transferor Company are transferred to the Transferee Company.

In such a scenario, various GST provisions come into play.

### Whether the transaction in the instant case involves supply of goods or supply of services?

Sr. No. 2 of Notification No. 12/2017- Central Tax (Rate) dated 28/06/17 exempts the following service from GST leviable thereon:

- *Services by way of transfer of a going concern, as a whole or an independent part thereof.*

Though the definitions of the terms 'goods' and 'services' as defined in the CGST Act, 2017 may create an anomaly as to whether transfer of a business is in the nature of goods or services, the above notification makes it aptly clear that if there is a transfer of a going concern, as a whole or an independent part thereof, the same is considered to be a supply of service. The same is exempt from levy of GST.

The view that the relevant transaction is a supply of service and is exempt from levy of GST is supported

by the following AARs:

- IN RE: M/S. PICO2FEMTO SEMICONDUCTOR SERVICES PRIVATE LIMITED 2023 (3) TMI 1114 - AUTHORITY FOR ADVANCE RULINGS, KARNATAKA
- IN RE: M/S. INNOVATIVE TEXTILES LTD. 2019 (4) TMI 1499 - AUTHORITY FOR ADVANCE RULINGS, UTTARAKHAND
- IN RE : M/S RAJASHRI FOODS PVT. LTD 2018 (5) TMI 1651 - AUTHORITY FOR ADVANCE RULING - KARNATAKA

At this juncture, the GST provisions pertaining to reversal as well as transfer of input tax credit (“ITC”) are analyzed.

### **Reversal of ITC**

If goods and services are used partly for providing taxable supply and partly for providing exempt supply, the amount of ITC is restricted only to so much of input tax which is attributable to taxable supply. This is evident from the provisions of Section 17(2).

Since the transaction in the instant case is that of “exempt supply” of service, it is required to be examined whether reversal of ITC is required. The manner of reversal is provided in Rules 42 and 43 of the Central Goods and Services Rules, 2017 (“CGST Rules, 2017”).

### **Transfer of ITC from the Transferor Company to the Transferee Company:**

*Section 18 of the CGST Act, 2017 pertains to “Availability of credit in special circumstances”. The provisions of Section 18(3) of the CGST Act, 2017 are as under:*

#### **Availability of credit in special circumstances.**

*(3) Where there is a change in the constitution of a registered person on account of sale, merger, demerger, amalgamation, lease or transfer of the business with the specific provisions for transfer of liabilities, the said registered person shall be **allowed to transfer** the input tax credit which remains unutilised in his electronic credit ledger to such sold, merged, demerged, amalgamated, leased or transferred business in such manner as may be prescribed.*

The procedure for such transfer is provided for under Rule 41 of the CGST Rules, 2017. The same is reproduced hereunder:

#### ***41. Transfer of credit on sale, merger, amalgamation, lease or transfer of a business.-***

*(1) A registered person shall, in the event of sale, merger, de-merger, amalgamation, lease or transfer or change in the ownership of business for any reason, furnish the details of sale, merger, de-merger, amalgamation, lease or transfer of business, in FORM GST ITC-02, electronically on the common portal along with a request for transfer of unutilized input tax credit lying in his electronic credit ledger to the transferee:*

*Provided that in the case of demerger, the input tax credit shall be apportioned in the ratio of the value of assets of the new units as specified in the demerger scheme.*

*Explanation: - For the purpose of this sub-rule, it is hereby clarified that the “value of assets” means the value of the entire assets of the business, whether or not input tax credit has been availed thereon*

*(2) The transferor shall also submit a copy of a certificate issued by a practicing chartered accountant or cost accountant certifying that the sale, merger, de-merger, amalgamation, lease or transfer of business has been done with a specific provision for the transfer of liabilities.*

*(3) The transferee shall, on the common portal, accept the details so furnished by the transferor and, upon such acceptance, the un-utilized credit specified in FORM GST ITC- 02 shall be credited to his electronic credit ledger.*

*(4) The inputs and capital goods so transferred shall be duly accounted for by the transferee in his books of account.*

In the AAR of IN RE: **M/S. B.M. INDUSTRIES [TS-886-AAR-2018-NT] - AUTHORITY FOR ADVANCE RULING, HARYANA**, it was held that since business was being transferred as a going concern, taking into account the provisions of Section 18(3) read with Rule 41, the applicant could transfer the unutilized input tax credit.

Taking into account the above-mentioned provisions, it is observed that Section 17 pertains to reversal of ITC if goods and/ or services are used partly for providing taxable supply and partly for providing exempt supply and Section 18 pertains to transfer of ITC.

The transaction is such as is covered both under Section 17 (since there is supply of exempt service) as well as Section 18. Considering the wordings of section 18, the Transferor Company is allowed to transfer the ITC and hence it may choose to do so out of choice and not compulsion. The intention of the law cannot be that the Transferor Company reverses the ITC attributable to exempt supply of service as well as transfers such ITC to the Transferee Company. Therefore, doing both reversal as well as transfer is ruled out.

Since the provisions of Section 17 (reversal) are general in nature, whereas those of Section 18 (transfer) are specific, if the Transferor Company opts to transfer the ITC to the Transferee Company, it may not reverse the same.

Contrary to the above view, the stance that the Transferor Company is liable to reverse the ITC as per the provisions of Section 17 and those of Rule 42 has been taken in the following AARs:

- IN RE: M/S. AIRPORTS AUTHORITY OF INDIA, 2023 (4) TMI 959 - AUTHORITY FOR ADVANCE RULING, RAJASTHAN
- IN RE: M/S. AIRPORTS AUTHORITY OF INDIA, CHAUDHARY CHARAN SINGH INTERNATIONAL AIRPORT, 2022 (7) TMI 642 - AUTHORITY FOR ADVANCE RULING, UTTAR PRADESH

In a scenario where a whole company is getting merged into another company, if the transferor company does not opt for transferring its ITC to the transferee company, it may reverse the entire ITC. It is worth noting that these AARs did not deliberate on section 18(3) and carried on the facts and discussions through the provisions of section 17 only. Moreover, there may arise practical issues of applicability of the provisions of Rule 42 (reversal of ITC pertaining to inputs and input services) in case of demerger of a company where the ITC is not transferred. This is because the value of exempt service might work out to disproportionately higher amount than that of taxable service and thereby a huge reversal of ITC may be required. Though this is a debatable issue.

#### Cancellation or suspension of registration of the Transferor Company

The provisions of Section 87 of the CGST Act, 2017 are required to be taken into account. The same are as under:

#### **Liability in case of amalgamation or merger of companies.**

*87. (1) When two or more companies are amalgamated or merged in pursuance of an order of court or of Tribunal or otherwise and the order is to take effect from a date earlier to the date of the order and any two or more of such companies have supplied or received any goods or services or both to or from each other during the period commencing on the date from which the order takes effect till the date of the order, then such transactions of supply and receipt shall be included in the turnover of supply or receipt of the respective companies and they shall be liable to pay tax accordingly.*

*(2) Notwithstanding anything contained in the said order, for the purposes of this Act, the said two or more companies shall be treated as distinct companies for the period up to the date of the said order and the registration certificates of the said companies shall be cancelled with effect from the date of the said order.*

It can be inferred from a conjoint reading of the above provisions alongwith those of Section 29 of the CGST Act, 2017 and Rules 20 and 21A(1) of the CGST Rules, 2017 that the Transferor Company should make application for cancellation of its GST registration in FORM GST REG-16 within 30 days of the merger coming into effect.

### **Registration requirements and liability of the Transferee Company**

In this regard, the provisions of Sections 22 and 85 of the CGST Act, 2017 are required to be taken into account. Section 22(4) requires the Transferee Company to be registered with effect from the date on which the Registrar of Companies issues a certificate of incorporation giving effect to the order of merger by the High Court or Tribunal. Moreover, it is worth noting that as per Section 85, the Transferor and the Transferee Companies shall, jointly and severally, be liable wholly or to the extent of such transfer, to pay the tax, interest or any penalty due from the Transferor Company up to the time of such transfer, whether such tax, interest or penalty has been determined before such transfer, but has remained unpaid or is determined thereafter.

Taking into account the above statutory provisions and discussion, the following steps may be taken by the Transferor and Transferee Companies:

#### **Actions to be taken by the Transferor Company:**

- In case the Transferor Company opts for transfer of ITC to the Transferee Company, it should file Form ITC-02 in order to transfer the ITC balance available in its electronic credit ledger. It would also require CA certificate certifying that the relevant merger/ transfer of business has been done with a specific provision for the transfer of liabilities.
- The Transferor Company shall surrender its GSTIN on account of being merged into the Transferee Company.

#### **Actions to be taken by the Transferee Company:**

- The Transferee Company should inform its vendors to issue tax invoices in the name of the Transferee Company (instead of the Transferor Company) in relation to the purchases made post the date of merger.
- The Transferee Company shall comply with all the GST provisions from the date of registration such as issuing of tax invoices, advance receipt vouchers and other tax paying documents, availing ITC for the purchases, discharging tax liability, filing of returns, etc.
- In case the Transferor Company has opted to transfer the ITC to the Transferee Company, the Transferee Company should, on the common portal, accept the details furnished by the Transferor Company and, upon such acceptance, the unutilized credit specified in FORM GST ITC-02 would be credited to its electronic credit ledger.
- The inputs and capital goods so transferred by the Transferor Company should be duly accounted for by the Transferee Company in its books of account.