



Business Structuring & Merger using LLP

At
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Bandra Kurla Complex ,
Mumbai

Presented by
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An Idea can change life , but ideas are no one's Monopoly!!!



LLP – News Paper Headlines

- Why is Mukesh Ambani shifting equity holdings in RIL to LLPs? Source: Economic Times
- Companies look at LLP's as new holding vehicle.
Source:Mint
- RBI-notification on exemption to smaller(less than 100 cr)
- Curbs no bar-Economic Times
- CA's may soon be able to form LLP's.



INDEX



- LLP - HISTORY TO CURRENT SCENERIO
- TAXATION OF LLP
- STRUCTURING OF LLP



Interesting Global History



- The concept of LLP originated in Italy.
- France is the first country which brought LLP under regulatory framework in 1673.
- In 1892, German Act on LLP extended the limited liability to all the partners.
- The Concept of Company is existing in UK since several Centuries.
- East India Company was formed in 1600BC
- First Joint Stock Companies Act was since 1844 in UK.



Background



- The concept of LLP originated in Italy.
- France is the first country which brought LLP under regulatory framework in 1673.

United States of America (US)

- Concept of LLP has its origin in 1991 (Texas statute)
 - Now adopted by almost every state in the US
 - Other “hybrid” entities: LPs, LLCs
- United Kingdom (UK)
 - LLP Act, 2000
 - Incorporated entity for legal purposes
 - Singapore
 - LLP Act, 2005: Similar to the UK legislation
 - Indian LLP mainly based on UK and Singapore LLP statutes



Why do we need separate form of Organization ?





Rationale



- There is a need for Multi Disciplinary Professionals Firm
- There is restriction on number of partners u/s. 11
- BIG Hurdle is the liability of all partners is unlimited
- SME can not cope up with corporate financial rigidity [i.e. Dividend, capital and related party transaction]
- SME can not cope up with compliance requirements in Company
- SME sector generally do not raise money from public



Who can prefer LLP?



- Asset Holding Companies
- Best for Joint Venture entities
- All partnerships /AOP with long term objective
- Professional Firms [CA/CS/CWA]
- Service sector/ Real Estate



Who can not go for LLP?



- Non profit making entities [NGO]
- Finance/ Investment entities [Till RBI recognises LLP]

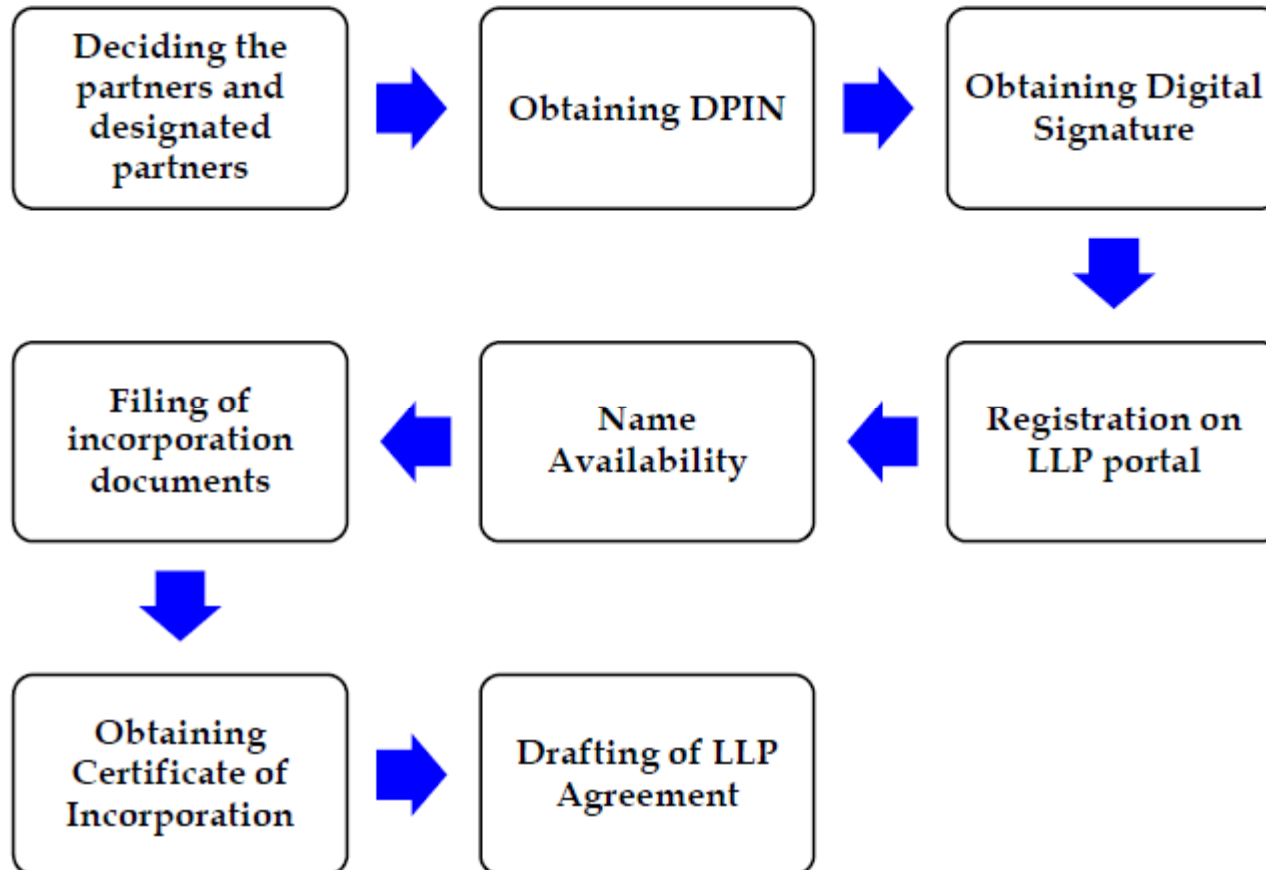


Indian LLP – A snapshot



- LLP Agreement governs an LLP
 - Contents of LLP Agreement largely in public domain; information on profit share ratio, remuneration/interest to partners remain confidential
 - Certain default provisions on equal share in capital, profits, participation in management of LLP apply unless LLP Agreement states otherwise
- Individual or body corporate can be a partner
 - “body corporate” includes foreign company; foreign LLP; another Indian LLP
- Partner can contribute tangible, movable or immovable or intangible property or other benefit

Formation of LLP





Important/ New Concepts in LLP



- Designated Partner
- Contribution
- LLP Agreement



Partners

- ❑ Minimum two individuals as partners who will be identified as Designated Partners.
- ❑ There is no upper limit for number of partners.
- ❑ Individuals, Foreign nationals, Indian Companies, Foreign Companies, Foreign LLP and Foreign LLC can become partner.
- ❑ In a case where corporate bodies are only partners at least two corporate bodies will have to nominate two individuals as partners who will be identified as Designated Partners.
- ❑ Government will issue guidelines for Foreign LLP and Foreign LLC to become partner in LLP. They will be governed by FEMA regulations.
- ❑ Minors cannot become partners of LLP.



Designated Partners



- Is a concept similar to officer in default
- Are like Directors with executive powers
- May be Partners Sharing Profit
- Partners if not designated will not be liable for any deeds of criminal offence committed by Designated Partners



Contribution

- May not be capital , but capital is contribution
- Is similar to guarantee
- Need not be the basis for voting/ control
- Need not be the basis for profit sharing



Imp. aspects of LLP Agreement

- Profit Sharing Pattern/ Voting/ Contribution may not be related
- Powers of DP and Partners to be specified
- Decision making process to be defined
- Exit mechanism / dispute resolution
- AOA of public co. can be the basis



Important features of First Schedule

- No partner shall draw remuneration
- LLP shall indemnify partner against liabilities incurred in Ordinary Course
- Each Partner shall have one vote at the meeting
- New partner can be admitted with consent of all the Partners
- Decision taken at Partners Meeting should be minuted within 30 days
- New business can be started with consent of all Partners
- Partner shall not compete with LLP
- Partner can not derive any benefit from LLP without consent of Partners

Comparison - LLP vs Partnership

LLP

- ❑ Minimum partners - 2
Maximum partners - unlimited
- ❑ A legal entity
- ❑ Registration is compulsory
- ❑ May have its own common seal
- ❑ Name has to be approved by the registrar and must have LLP as suffix
- ❑ Agreement available for inspection
- ❑ Can hold property in its own name
- ❑ Foreign nationals can be partners
- ❑ Liability is limited. Partner is liable only to the extent of agreed contribution and not for any independent/ unauthorized act of other partners

Partnership

- ❑ Minimum partners - 2
Maximum partners - 20
- ❑ Not a legal entity
- ❑ Registration is optional
- ❑ No concept of common seal
- ❑ Any name of its choice
- ❑ Deed not available for inspection
- ❑ Cannot hold property in its own name
- ❑ Foreign nationals cannot be partners
- ❑ Liability is unlimited. Partner is jointly and severally liable for all the acts of the firm and its other partners

Comparison - LLP vs Partnership

LLP

- ❑ Relationship of Partner and LLP and partner inter-se depends upon terms of LLP agreement
- ❑ Provisions of Indian Partnership Act, 1932 not applicable
- ❑ Is a legal entity which can be sued as well as it can sue the third party
- ❑ Minor cannot become partner

Partnership

- ❑ Partner can act as an agent of the firm as well as agent of the other partners
- ❑ Provisions of Indian Partnership Act, 1932 applicable
- ❑ Legal proceedings can be taken against a partnership firm irrespective whether it is registered or not. Only registered partnership firm can take legal recourse or defend legal proceedings
- ❑ Minor can be admitted to the benefits of partnership

LLP VS Company

LLP	COMPANY
1. Ownership and Management can be with same person or can be divorced .	1. Ownership and management is divorced.
2. LLP can be borrowed from any person	2. Company can not borrow from shareholder/ Relatives etc. (Section 73-75).
3.No such restriction under LLP	3. Company can not lead to other entity in which Directors are interested . (Sec 185-186)
4. No such restrictions	4. Company can not accept any amount (Deposit/ Advances) after 12 months (Section 73-75)

LLP VS Company

LLP	COMPANY
5. Operational structure has more flexibility Eg. change in terms of partnership, change in profit sharing ratio, remunerating the partners, introduction and withdrawal of capital, dissolution of LLP etc.	5. Operational Structure has less flexibility.
6. Statutory compliance easy approval by partners only	6. Statutory Compliance complex approval by BOD's / Shareholders.
7. Accounts can be maintained either on cash or mercantile system.	7. Accounts have to maintained on mercantile system.

Lifting up Curbs on LLPs



Red carpet for foreign investors

LLPs are biz organisation, a hybrid between cos & partnership firms with reduced statutory requirements

THEY are seen as an attractive vehicle by foreign investors to route their investments

What is being proposed?

AUTOMATIC access to foreign investors via LLPs in sectors where 100% FDI is permitted

PERMIT entry in sectors with caps with prior FIPB approval.

What is the current regime?

LLPs have a restricted FDI regime. ?

FOREIGN investors need prior FIPB nod in sectors on the automatic route

FOREIGN investment via LLP not permitted in sectors with caps

DIPP is in discussion with finance and corporate affairs ministries



RBI has already given a go-ahead with some checks



The foreign investment policy for LLPs is being reviewed. There is a need to align with the policy for companies, said a government official

Source : Economic Times Dated 3 October 2014



FDI framework - General

- FDI generally understood to mean investments by way of equity shares, fully convertible preference shares and convertible debentures
- Broadly, FDI permitted under 2 routes:
 - Automatic route - No prior permission, only requirement to inform RBI within 30 days of inflow / issue of shares
 - Approval route - prior approval of the Foreign Investment Promotion Board (FIPB), Ministry of Finance, Government of India (GOI) required
- Until recently, FDI allowed into “Indian Company” only in its “capital instruments” i.e. Equity Shares, Compulsory Convertible Preference Shares (CCPS) and Compulsory Convertible Debentures (CCDs)



FDI framework – recent developments

- May 2011: Cabinet Committee on Economic Affairs (CCEA) of the GOI approves proposal to allow FDI on LLPs
 - Implementation in a calibrated manner, starting with “open” sectors and subject to conditions
- May 2011: GOI issues Press Note 1 of 2011 for implementing the CCEA approval



FDI framework – recent development



- Press Note No 1 of 2011
 - 100% FDI permitted in LLP with **prior approval** of FIPB in sectors where 100% FDI is allowed under automatic route
 - FDI in LLP **not** permitted in the following sectors
 - FDI-linked performance condition is attached (minimum capitalization, lock-in period, etc)
 - Prohibited sectors like agricultural/ plantation activity, print media or real estate business
 - FII /FVCI not permitted to invest in LLPs
 - LLPs **not** permitted to avail External Commercial Borrowings (ECBs)
 - Conversion of company with FDI into LLP permitted, but prior approval of FIPB required and under similar conditions



FDI framework – recent developments



- **Press Note No 1 of 2011 (Cont'd)**
 - **LLPs with FDI **not** eligible to make any downstream investments**
 - **Indian companies with FDI permitted to make downstream investment in LLPs only if both the Indian company and the LLP operate in sectors where 100% FDI is permitted under automatic route and no FDI-linked conditions attached**
 - **Capital contribution by partner only in cash**
 - **Designated Partners (DPs) in LLPs with FDI**
 - **For the purposes of appointing a DP, “resident in India” would have the meaning, as defined for “person resident in India”, under FEMA**
 - **Where an LLP wants to have a body corporate as a DP, only a company registered in India under the Companies Act, 1956 can be a DP**
 - **DP responsible for compliance with the FDI conditions and liable for all penalties imposed on the LLP for any contravention.**



Opportunities for CAs

- Incorporation of LLP
- Drafting of LLP Agreement [V V IMP]
- Conversion of Partnerships into LLP
- Conversion of Private or Closely held Public Ltd cos' into LLP
- Compliance services for LLP
- Gearing up for Multi Disciplinary Practice



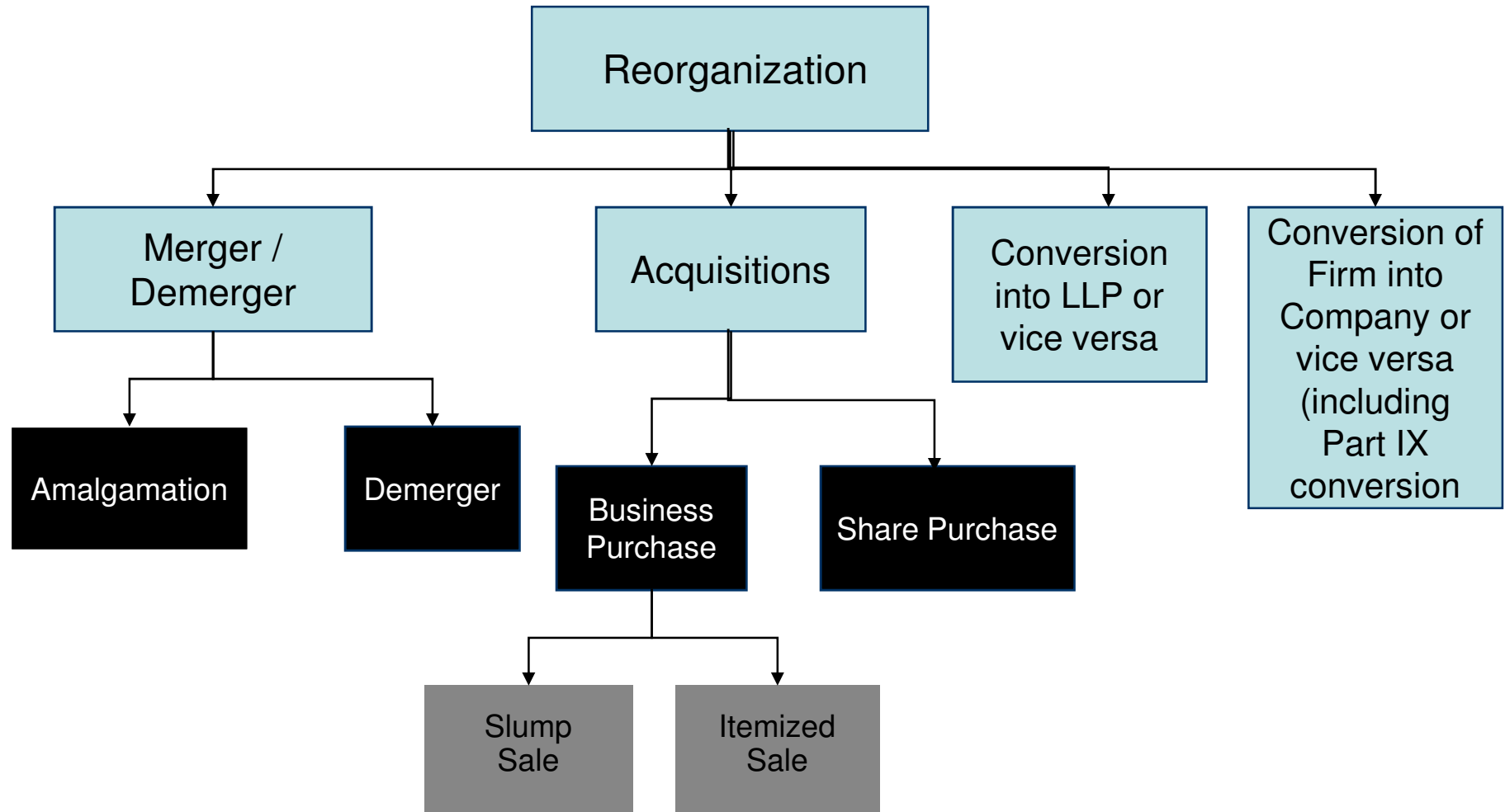
Why Structuring?



- **Enhance shareholder value**
- **Grow inorganically**
- **Overcome threat / competition**
- **Achieve economies of scale / synergies**
- **Exit non-core businesses**
- **Re-direct capital to core competencies**
- **As a part of global / group restructuring**



Modes of Reorganization in India





Taxation Coverage



Taxation

- Corporatization of corporate entity
- Conversion as per Part IX Route
- LLP conversion of unlisted corporate entity
- Explanatory Notes
- Alternate Minimum Tax (AMT)

LLP Corporatization of corporate entity

o Exemption u/s 47(xiii) 47(xiv) subject to fulfillment of certain conditions

o All the partners of the firm become the shareholders of the company in the same proportion

o No consideration other than issue of shares in the company

o All the assets and liabilities of the proprietary concern or the firm are transferred

o The aggregate shareholding of the proprietor or partners is not less than 50% of total voting power in the company and continue for period of five years



Conversion as per Part IX Route



- o Becomes corporate entity by process of law
- o Held by various courts since no 'transfer' no tax implications
- o Texspin Eng & Mfg Works (263 ITR 345) (Bom HC)
- o Recent ruling of AAR in the case of Umicore Finance Luxembourg (318 ITR 78) (AAR)
- o Stamp duty not payable?



LLP Conversion of Unlisted corporate entity



- Condition for Capital Gain Exemption Sec 47 (xiiib) :
- All assets and liabilities of the company become the assets and liabilities of the LLP
- Shareholders of the company become partners of the LLP in the same proportions as their shareholdings in the company.
- No consideration other than share in profit and capital contribution in the LLP arises to partners.
- The erstwhile shareholders of the company continue to be entitled to receive at least 50 per cent of the profits of the LLP for the period of five years from the date of conversion.
- Total sales turnover or gross receipts in business of the company do not exceed Rs.60 lakh in any of the three preceding previous year.
- No amount is paid, either directly or indirectly to any partner to any partner out of the accumulated profit of the company for a period of three years from the date of conversion



Income-tax : Explanatory Notes to the provisions of the Finance Act, 2010

- The total sales, turnover or gross receipts in business of the company
[which are taxable under the head "Profits and gains of the business or profession"]

do not exceed sixty lakh rupees in any of the three preceding previous years; and

[F.No. 142/1/2011-SO(TPL)]

VIOLATION OF CONDITION U/S 47(xiiib)

Aravali polymers LLP V JCIT (Kolkata)

Appeal No. 242/CIT(A)-xx/Range 34 Dt. 10.04.2014

- LLP Post Conversion gave Interest free loan to partners from Reserves & Surplus before conversion.
- This amounts to violating of proviso (f) of section 47 (xiiib).
- Due to violation provisions of section 47A(4) did not apply.
- Capital gain Exemption claimed on conversion revoked & remanded book for re-computation u/s 45 (i.e. without exemption)



Alternative Minimum Tax (AMT)

- Where the regular income-tax payable for a previous year by a limited liability partnership is less than the alternate minimum tax payable for such previous year, **the adjusted total income** shall be deemed to be the total income of such limited liability partnership and it shall be liable to pay income-tax on such total income at the rate of eighteen and one-half per cent..
- For the purpose of the above,
 - (i) “Adjusted total income” shall be the total income (Taxable Income) as increased by :
 - a) The deductions claimed under any section included in Chapter VI-A under the heading “C – Deductions in respect of certain incomes ” (pertaining to deductions for Infrastructure , Hotel, Industrial Undertaking etc) and
 - b) Deduction claimed under section 10AA (pertaining to Special Economic Zone);

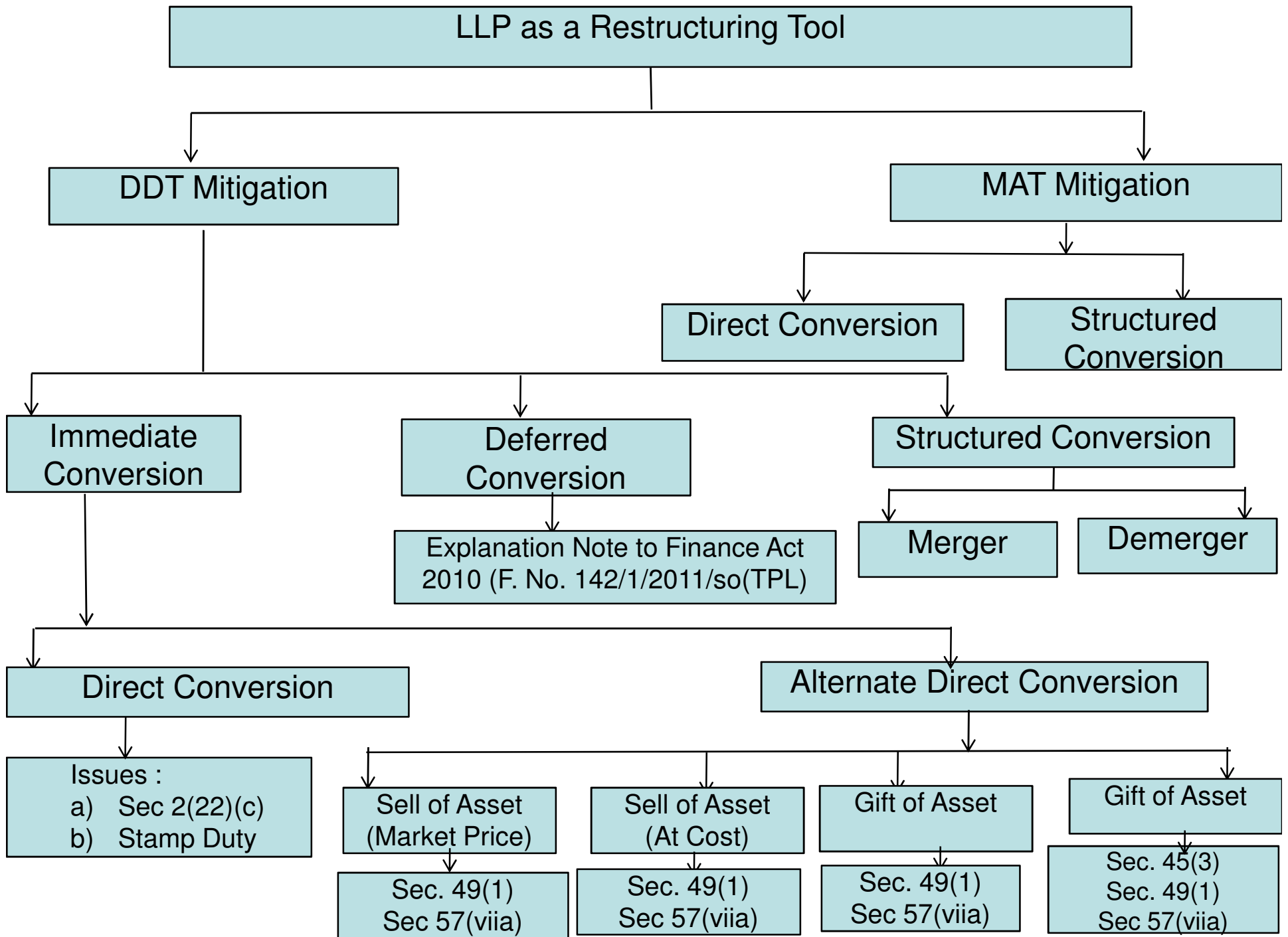


Comparison:



AMT (LLP) and MAT (Company)

AMT	MAT
<ul style="list-style-type: none">• Linked to total income as adjusted for deductions u/s 10AA and under Ch. VI-A• Investment linked tax holiday cases protected• Incomes exempt u/s 10 beyond purview of AMT• Quantum of carried forward losses does not impact AMT	<ul style="list-style-type: none">• Linked to 'Book Profit' as modified for specified downward / upward adjustments• Investment linked tax holiday cases subject to MAT• STT paid LTCG subject to MAT• Restrictive set off of book losses of earlier years





Why is Mukesh Ambani shifting equity holdings in RIL to LLPs?

Source: Economic Times

Here is what's behind the move:

In conventional partnership firms, partners have unlimited liability i.e. their personal assets can also be called in to service liabilities of the firm.

Neither RIL nor Mr Ambani are disclosing the reason. But tax experts said it would make the shareholding more tax efficient.





Declaration in Stock Exchange



FORM C
 Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992
 [Regulation 13(3) and (6)]

Regulation 13(3) – Details of change in shareholding in respect of persons holding more than 5% share in a listed company

Name, PAN, & address of shareholders	Shareholding prior to acquisition / sale	No. and % of shares/voting rights acquired / sold	Receipt of allotment advice / acquisition of shares / sale of shares specify	Date of intimation to Company	Mode of acquisition (market purchase/ public/rights/preferential offer etc.) / sale	No. & % of shares / voting rights post acquisition / sale	Trading member through whom the trade was executed with SEBI Registration No. of the TM	Exchange on which the trade was executed	Buy quantity
Kankal Investments And Trading Company Private Limited- PAN - AAACK1771A, Address: 54-A, Model Court, 224, Nariman Point, Mumbai 400 021.	31,38,90,640	Shares transferred 18,53,09,688 5.33% (VR)	Date of transfer - 11-08-10	13-08-10	Off-market	14,84,90,952 - 4.79%(VR)	Not Applicable	Not Applicable	100
		Shares acquired-100 (0.00%)(VR)	Date of acquisition - 11-08-10						

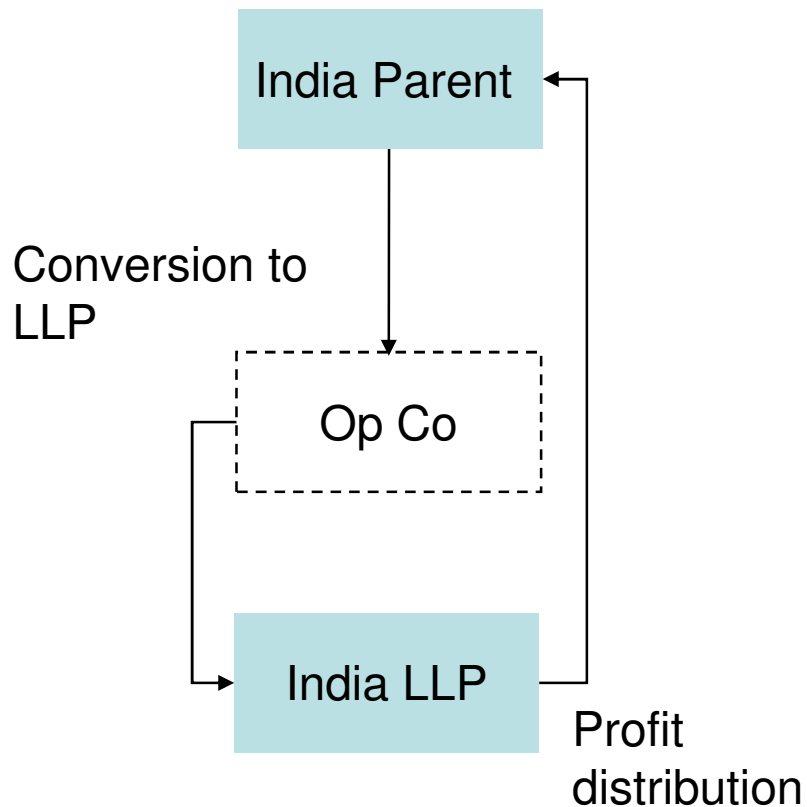
Note: The transfer & acquisition is part of the inter-se transfer without consideration amongst "group".

For Kankal Investments And Trading Company Private Limited

Director / Authorized Signatory

Date: 13-08-10

Option 1 – Operating company converted to LLP

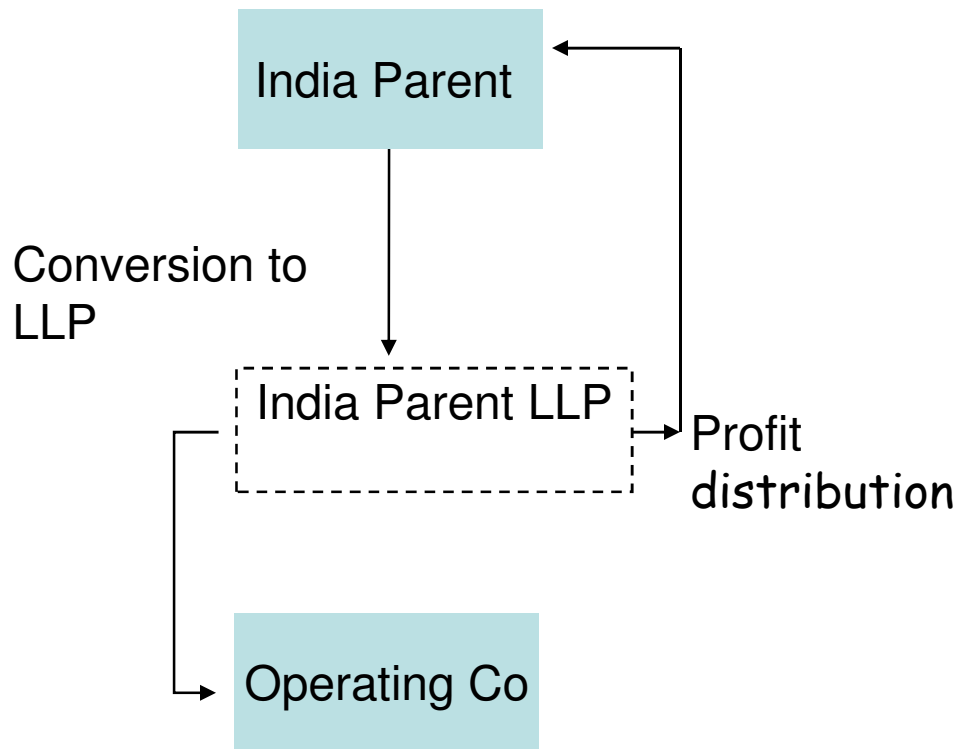


- **Description**
 - Operating company converted to LLP
 - Indian parent is partner in LLP
 - LLP distributes profits to partners
- **Benefits**
 - No DDT
 - Profits exempt in hands of Indian parent
- **Issues**
 - Tax implications upon conversion of existing company into LLP.
 - Compliance requirements for “partnership treatment”



Option II

Holding company converted to LLP



- **Description**
 - Indian Parent company converted to LLP
 - LLP distributes profits to partners
- **Benefits**
 - No DDT
 - Profits exempt in hands of Indian parent
- **Issues**
 - Tax implications upon conversion of existing company into LLP.
 - Compliance requirements for “partnership treatment”



DIRECT CONVERSION



ABC LTD

	2007-08	2008-09	2009-10
Sales	80	20	20
Sh. Capital	1	1	1
Reserve			
P&L	(30)	(30)	(30)

XYZ LTD

	2007-08	2008-09	2009-10
Sales	20	30	30
Sh. Capital	1	1	1
P&L	20	25	30
Reserve			



Section 2(22)(c) - Applicability

- dividend" includes
- any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not ;



View Published in one Book

- On Conversion of Pvt Ltd co. To LLP
- a) There is exemption to shareholder u/s 47 (xiiib)
- b) However, any distribution by co.out of accumulated profit to shareholder at the time of liquidation amount to dividend by virtue of sec 2 (22) (c)
- c) Due to the applicability of sec 2 (22) (c)the provision of dividend will be applicable and shareholder has to pay tax on the same
- d) Dividend amount will be the Extent of the accumulated profit after Tax



Alternate View



- **If Sec 2 (22) (c) is applicable to sonversion of private ltd company into LLP than**
 - (1) The said analogy should be applied to ALL MERGER and DEMRGER cases.
 - (2) In fact in case of Merger , there is LIQUIDATIONS of AMALGAMATING COMPANY. (All the Provision of Liquidation Applicable) and these is not case with LLP Conversation(No Provision relating to liquidation applicable) to LLP
 - (3) In case of LLP Conversion there is No Liquidation under companies Act. Only Deemed liquidation under LLP Act.
 - (4) Supreme Court in case of Hari Prasad Jayantilal & Co.Vs V.S.Gupta (59 ITR 794) (SC) - this is in connection with definition as Dividend .In that Court has held that Dividend means Dividend as ordinarily understood under Companies Act.
 - (5) Its Like Registration of Co under LLP. (Like Part IX Conversion)
 - (6) Bombay High court in case TEXSPIN Eng & Mfg Works (263 ITR 345)
 - (7) Also there is NO DISTRIBUTION to share holder.



Mitigating 2 (22) (c).



- Merge profit making co. with loss making co. or co. with NIL profit.
- This exercise is needed to transfer FREE accumulated profit to the character of non accumulated profit (by high court scheme.)
- In present case position of ABC post merger will be in example :

ABC CO.

	2010-11	2011-12	2012-13	2013-14
Sales	80	20	20	50
Sh. Capital	1	1	1	2
Reserve				30
P&L				(30)

Now, ABC Ltd can converted into LLP as there will be Nil accumulated profits as per sec 2 (22) (c).

Stamp Duty Implications

- ❑ Company having immovable property when converted into LLP, whether there is liability for payment of stamp duty ?
- ❑ As per Section 58 of LLP Act, 2008, all the assets and liabilities vest into LLP. There is no transfer of assets and liabilities.
- ❑ As per decision of Bombay High Court in the case of Taxpin Engg.& Mfg. Works and A.P. High Court in the case of Vali Pattabhirama Rao vs. Shri Ramanuja Ginning & Rice Factory (P) Ltd. when the firm is converted into company under Part IX of Companies Act, 1956, the assets of the firm vest into the company and there is no transfer. Whether the ratio of these decisions can be applied on the issue of payment of stamp duty ?
- ❑ If LLP does not pay stamp duty and continues to enjoy the property being registered in the name of company, can the title of the property be considered as defective ? Whether at the time of sale of such property any issue can arise ?



ALTERNATE DIRECT CONVERSION



EXISTING SCENERIO



ABC LTD (HOLDING
COMPANY)

P&L

PARTICULARS	AMT	PARTICULARS	AMT
EXPENSES	5	DIVIDEND	100
NET PROFIT	95		
	100		100

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	INVESTMENT	1000
RESERVE	900	(MV-100000)	
	1000		1000



Holding Co. LLP Conversion Options

- 1) IF ABC SALES ALL SHARES (At Market rate) THROUGH MARKET TRANSACTIONS and INTRODUCED AS CAPITAL
- 2) IF ABC SALES ALL SHARES (At Cost) THROUGH OFF MARKET TRANSACTIONS(AT COST)
- 3) IF ABC GIFT ALL SHARES THROUGH OFF MARKET TRANSACTIONS
- 4) INTRODUCES THE SHARES AT COST AS CAPITAL INTO XYZ LLP



OPTION 1



a) IF ABC SALES ALL SHARES THROUGH STOCK EXCHANGE

b) INTRODUCES THE NET CONSIDERATION RECEIVED AS CAPITAL INTO XYZ LLP

ABC LTD

P&L

PARTICULARS	AMT	PARTICULARS	AMT
EXPENSES	5	CAP GAIN	99000
MAT @ 17%	16830		
NET PROFIT	82165		
	99000		99000

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	CAPITAL WITH	83165
OP RESERVE	900	XYZ LLP	
ADDITION	82165		
	83165		83165



**XYZ LLP
BALANCE SHEET**

ASSET	AMT	LIABILITIES	AMT
CAPITAL	83165	INVESTMENT	100000
LOAN	16835		
	100000		

REMARK

**NOT COST EFFICIENT AS HUGE OUTFLOW ON
ACCOUNT OF MAT**



Option 2

ABC Sales shares at Cost Rs. 1000 (MV 1,00,000) to XYZ
LLP

ABC LTD

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	BANK	1000
RESERVE	900		
	1000		1000

XYZ LLP

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	1000	INVESTMENT(M.V.1000 00)	1000
	1000		1000



Section 56 (2)(viiia)



Where a firm or a company not being a company in which the public are substantially interested, receives, in any previous year, from any person or persons, on or after the 1st day of June, 2010, any property, being shares of a company **not being a company in which the public are substantially interested**



Option 3 (Gift)

ABC GIFT shares at costing Rs. 1000 (MV 1,00,000) to
XYZ LLP

ABC LTD

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	PROFIT AND LOSS	1000
RESERVE	900		
	1000		1000

XYZ LLP

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	NIL	INVESTMENT(M.V.100000)	NIL
	NIL		NIL



Section 2(42A) [Short Term/ Long Term]

- **[Explanation 1].—(i) In determining the period for which any capital asset is held by the assessee—**
 - **(a) in the case of a share held in a company in liquidation, there shall be excluded the period subsequent to the date on which the company goes into liquidation ;**
 - **(b) in the case of a capital asset which becomes the property of the assessee in the circumstances mentioned in 7[sub-section (1)] of section 49, there shall be included the period for which the asset was held by the previous owner referred to in the said section ;**



Section 49(1)



[(1)] Where the capital asset became the property of the assessee

(i) on any distribution of assets on the total or partial partition of a Hindu undivided family;

(ii) under a gift or will;

(iii) (a) by succession, inheritance or devolution , or

[(b) on any distribution of assets on the dissolution of a firm, body of individuals, or other association of persons, where such dissolution had taken place at any time before the 1st day of April, 1987, or]

(c) on any distribution of assets on the liquidation of a company, or

(d) under a transfer to a revocable or an irrevocable trust, or

(e) under any such transfer as is referred to in clause

(iv) or clause (v)] [or clause (vi)] [or clause (via)] [or clause (viaa)] [or clause (vica) or [clause (vicb)] of section 47]; Clause (xiib) of section 47



I-T notice to Shah Rukh



Khan over 'gifted' Dubai villa

- The department alleged that for other endorsements, Khan was charging huge amounts as shown in his returns.
- 'The company is an artificial juristic person devoid of any natural senses such as love and affection. This rules out the concept "natural love and affection" and "without any consideration" which are vital elements to characterize the gift," said the demand notice.



(Source : Economic Times, dated 10/01/2011)



Option 4 (Capital Introduction)



ABC INTRODUCE shares at cost Rs. 1000 (MV 1,00,000)
to XYZ LLP

ABC LTD

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	CAPITAL WITH	1000
RESERVE	900	XYZ LLP	
	1000		1000

XYZ LLP

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	1000	INVESTMENT	1000
	1000		1000



Company as a partner in LLP



Contribution of investments at book value Sec 45(3)

It saves future MAT and DDT on funds generated and long term capital gain earned on sale of such transfer portfolio

- it may save liability on dividend distribution , if any under Sec2(22) (c)
- Date of holding for investments for LLP starts from date introduction as capital.(Where as in case of gift - of holding by erst while pvt ltd co. (Sec 49 (1)(e) r.w.s 2(42A) will be considered and hence long term)
- Whether interest payment on capital account balance of company as partner is fatal to claim for LTC exemption???



Section 45 (3)

- **Capital asset transferred by the partner to the partnership firm:** As per section 45(3) of the Income Tax Act 1961 if any partner in a firm transfers his asset to the firm then the capital gain on such asset as arising to the partner shall be calculated by presuming the sale value of such asset as is recorded in the books of accounts of the firm and not the market value of the asset.



Definition Of Income sec 2(24)(iv)



- The value of any benefit or perquisite, whether convertible into money or not, obtained from a company either as a director or by a person who has a substantial interest in the company , or by a relative of a director or such person , and any sum paid by such a company in respect of any obligation which , but for such payment, would have been payable by the director or other person aforesaid.



Alternate Direct Conversion Analysis

	Trf At Mkt Value	Trf at Cost	Trf as Gift	Capital introduction
MAT Applicable	Yes	No	No	No
Benefit of LTCG will be available to LLP on conversion	No	No	Yes	No
Gift provision applicable Sec 56(7)	No	No	No	No

Deferred Conversion

▪PQR Pvt. Ltd. want to convert in to LLP .

Following Facts

▪Company also operate similar business from other sister concern

▪Company has Properties and Shares with high Market Value

▪Company Does not wish to sell any of the Investments

▪Company wish to save DDT and MAT and Stamp Duty

PQR Private Ltd (Rs in crore)				
Source of Income	2010-11	2011-12	2012-13	2013-14
Sales	1	1.15	1.35	1.5
Rent	5	5.10	5.15	5.35
Capital Gain	1.25	1.40	1.65	2.05
Other Sources	1.75	1.95	2.15	2.5
Total	9	9.60	10.30	11.40

Deferred Conversion

▪PQR Pvt. Ltd. Has to project following actions for converting to LLP .

ACTIONS

- Company should discontinue BUSINESS operations by shifting to sister concern OR reduce it to below 60 Lacs
- Other Activities i.e Renting , Investments etc (Not taxable under the HEAD BUSINESS and Profession)can be continue
- By vertue of Explanatory Memorandum to Finance Act 2010 (F.N.142/1/2011.) it will qualify for conversion

PQR Private Ltd		(Rs in crore)		
Source of Income	2014-15	2015-16	2016-17	
Sales	0.55	0.45	0.35	
Rent	5.5	5.65	5.95	
Capital Gain	1.25	1.40	1.65	
Other Sources	1.75	1.95	2.15	
Total	9	9.60	10.30	

STRUCTURED CONVERSION





CASE STUDY ON STRUCTURED CONVERSION



Balance Sheet of A Pvt. Ltd (With Sales Exceeding Rs.60 Lacs for last 3 yrs)

Liability	Amount	Assets	Amount
Share Capital	10000	STOCK - IN TRADE	10000
Reserve	0		
Total	10000	Total	10000

Balance Sheet of B Pvt. Ltd (With Sales Less Than Rs.60 Lacs for Last 3 Yrs)

Liability	Amount	Assets	Amount
Share Capital	1000	Investments	10000
Reserve	9000		



Merger



What is a Merger?

- **Merger refers to consolidation of two or more entities**
- **Involves transfer of assets and liabilities from one or more transferor companies to a transferee company**
- **In consideration, typically the transferee company issues shares to the shareholders of transferor company**
- **Process (4-6 months):**
 - **High Court approval (Section 391-394 of Companies Act)**
 - **Central Government approval (Section 395 of Companies Act)**
 - **BIFR Approval (Sick Industrial Companies Act)**
 - **Banking Regulations**



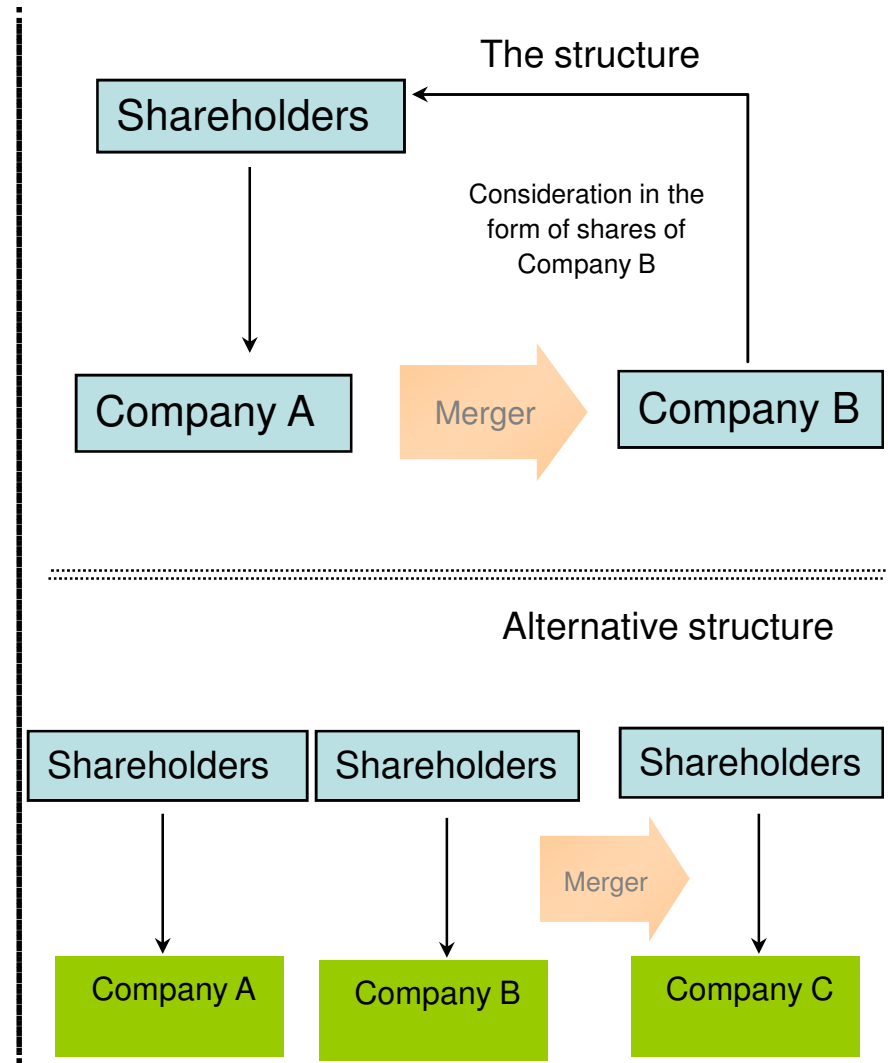
Amalgamation - Definition



Section 2(1B)

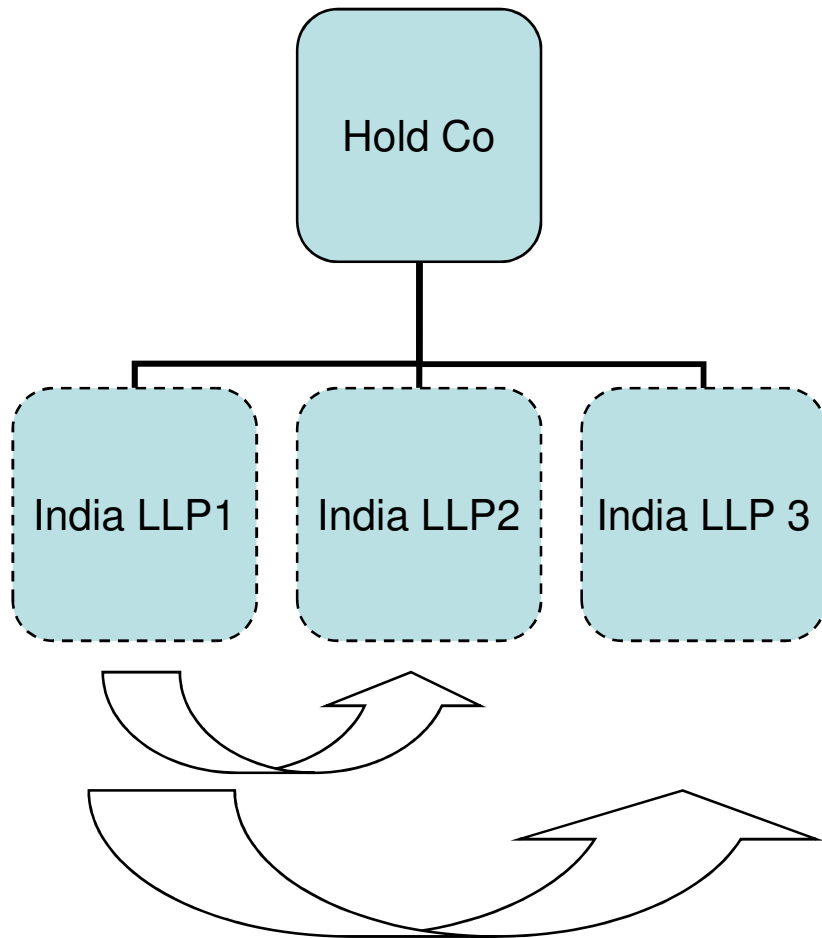
- o Definition of amalgamation-
 - o All properties to be transferred to the merged company
 - o All liabilities to be transferred to the merged company
 - o At least 3/4th in value of shareholders of the merging company (excluding shares already held by the amalgamated co.) should be shareholders of the merged company
 - o *The above conditions are*

The merger is tax neutral only if all above conditions are met





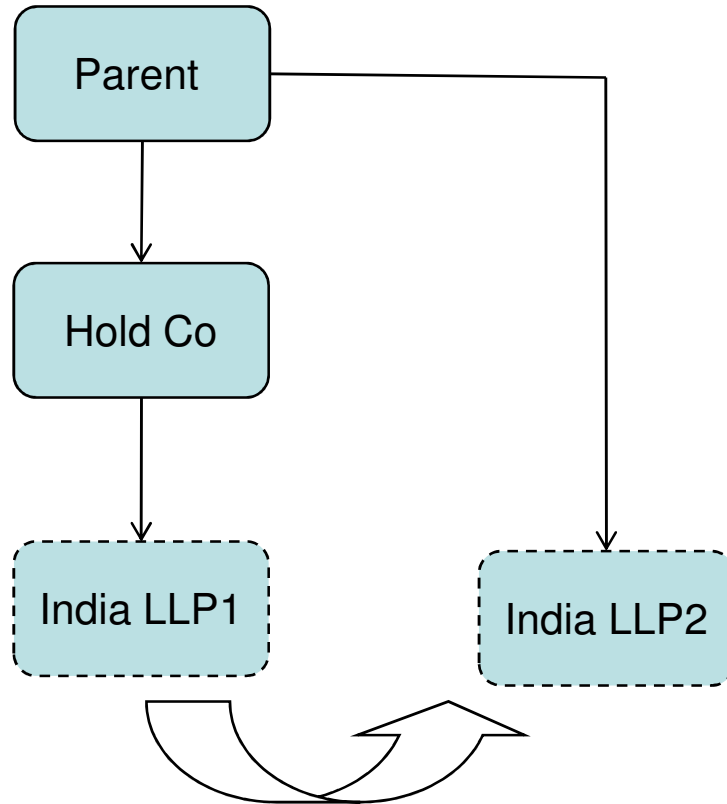
Deemed Dividend Mitigation - WITHOUT CONVERSION



- Description
 - Indian Holding company with multiple Indian operating entities
 - Indian operating entities set up as LLPs
 - Excess cash in one operating entity and need for cash in another
 - Inter-LLP loan
- Benefits
 - Inter-LLP not considered as deemed dividend
 - Tax efficient movement of ⁷² cash within operating entities



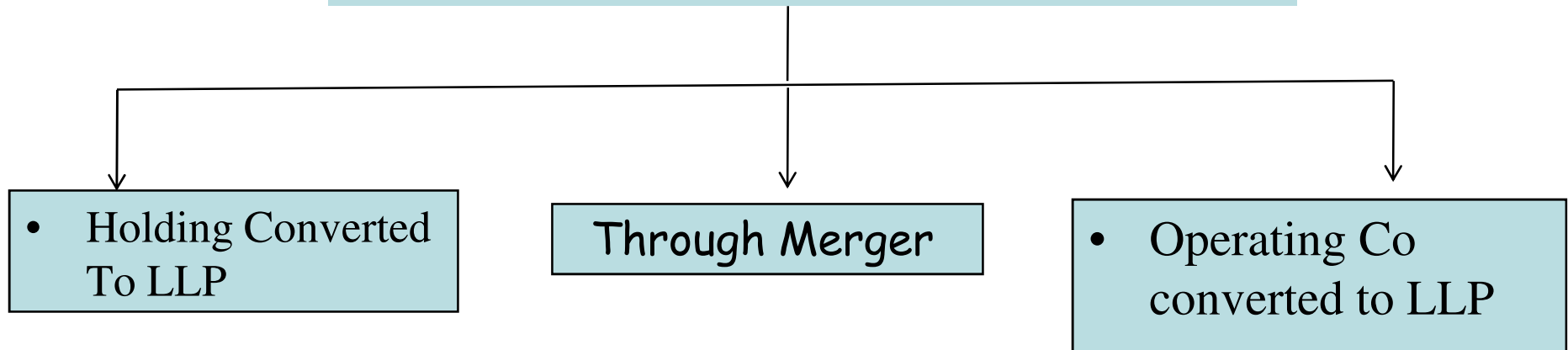
Deemed Dividend Mitigation - Variation



- **Description**
 - Parent with cash rich subsidiary (Hold Co) in high tax jurisdiction
 - Indian operating entity for Parent set up as India LLP2
 - Excess cash sitting in Hold Co and need for cash in India LLP2
 - India LLP1 formed with Hold Co as a partner,
 - Cash divested in India LLP1 as capital contribution
 - Inter-LLP loan
- **Benefits**
 - Inter-LLP loan not considered as deemed dividend
 - Tax efficient movement of cash
- **Issues**
 - FDI restrictions need to be considered
 - India LLP 1 should not pursue NBFC covered activity and should not be a conduit



MAT MITIGATION





MAT PLANNING (Mitigation)



Option 1 : Plain Conversion of Pvt Ltd Co. into LLP

ABC Holding Pvt. Ltd.

Profit & Loss A/c

Particulars	Amt	Particulars	Amt
Expenses	5	Sales	55
Net Profit	50	(less than 60 L)	
	55		55

Balance Sheet

Particulars	Amt	Particulars	Amt
Sh Cap	100		
Reserve	900	Investment (M.V.10,000)	1000
	1000		1000



Option II - Through Merger



(if RBI permission is required)

Existing position

ABC LTD

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	INVESTMENT(M.V.10000)	1000
RESERVE	900		
	1000		1000

XYZ Pvt ltd

BALANCE SHEET

ASSET	AMT	LIABILITIES	AMT
CAPITAL	100	BANK	100
	100		100



Companies look at LLP's as new holding vehicle.



Source: Mint

- Aravali Polymers, one of the holding firms of EIH Ltd that sold a stake to Reliance Industries Ltd (RIL) on Monday, had been classified as a private limited firm on the Bombay Stock Exchange (BSE) until the June quarter.
- In its announcement on Monday, Aravali Polymers was categorized as an Llp firm, which will help it save taxes.

Source: Mint Newspaper dated 26/08/2010



VIOLATION OF CONDITION U/S 47(xiiib)

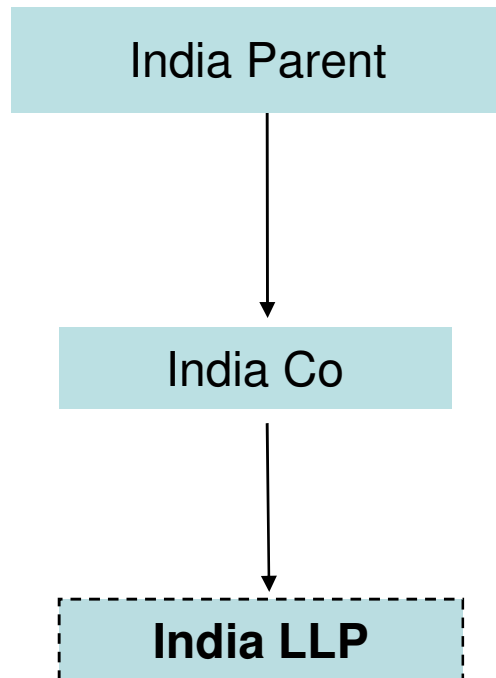
Aravali polymers LLP V JCIT (Kolkata)

Appeal No. 242/CIT(A)-xx/Range 34 Dt. 10.04.2014

- LLP Post Conversion gave Interest free loan to partners from Reserves & Surplus before conversion.
- This amounts to violating of proviso (f) of section 47 (xiiib).
- Due to violation provisions of section 47A(4) did not apply.
- Capital gain Exemption claimed on conversion revoked & remanded book for re-computation u/s 45 (i.e. without exemption)



MAT planning, existing business option I

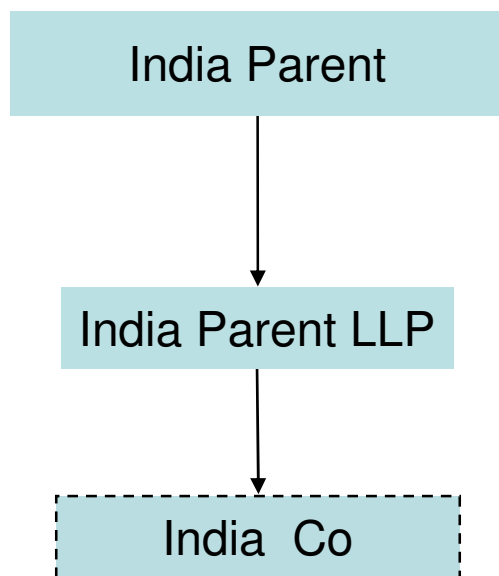


Description

- India Co belongs to an Indian owned group
- India Co transfers its tax holiday business (STP/ EOU Unit) to India LLP
- India Co is a partner in India LLP
- **Benefits**
 - Profits earned by LLP eligible for tax holiday
 - MAT not applicable to LLP
 - Distribution by LLP tax exempt in India Co's hands and not subject to MAT for India Co
- **Issues**
 - Compliance requirements for "partnership treatment"
 - Eligibility of transferee / successor LLP to claim deduction under incentive provision.



MAT planning, existing business



- **Description**
 - India Co belongs to an Indian owned group
 - India Parent converted in to LLP
- **Benefits**
 - Dividend Distributed by Indian Company and received by LLP eligible for tax holiday
 - MAT not applicable to LLP
 - Distribution by LLP tax exempt in India Co's hands and not subject to MAT for India Co
- **Issues**
 - Compliance requirements for "partnership treatment"
 - Eligibility of transferee / successor LLP to claim deduction under incentive provision.



MAT PLANNING CONTD....



Balance Sheet of ABC LLP (Post Conversion)

Particulars	Amt	Particulars	Amt
Partners Capital Contribution	100	Investment	1000
Reserve	900		
	1000		1000



Position After Sale of Investments

ABC HOLDING LLP

Profit & Loss A/c

Particulars	Amt	Particulars	Amt
Net Profit	9000	Capital Gain (Both LT & ST)	9000
	9000		9000

Balance Sheet

Particulars	Amt	Particulars	Amt
Partners Capital	100	Bank	10000
Add: Profit	<u>9000</u>		
Reserve	900		
	<u>10000</u>		



Proposed :- ABC merged with XYZ at purchase method.

- Now , MAT impact will be NIL or minimum till xyz sell shares at 10000. Because book profit will be computed as per schedule VI. Due to this :
 - Cost of shares will restated (revalued) in the books of XYZ due to high court order.
 - This will result in lower or Nil book profit.
 - Hence Nil or minimum MAT liability.

XYZ Co

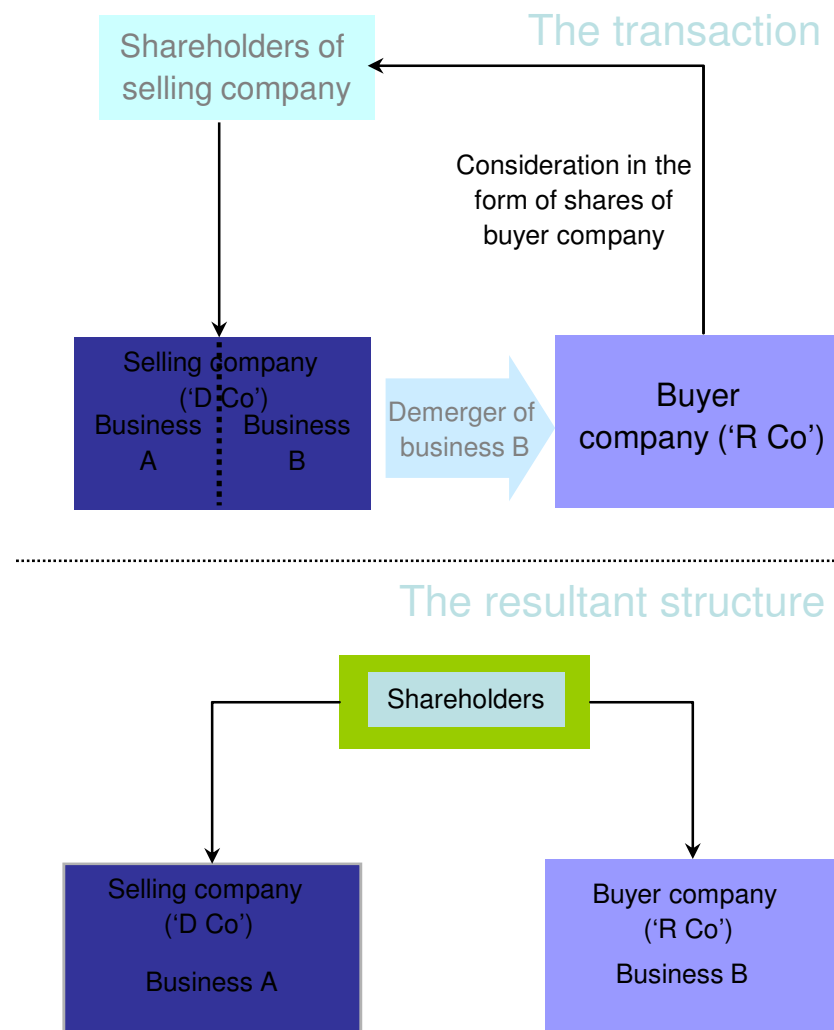
Liabilities	Amt	Assets	Amt
Capital	200	Investment	10000
Reserve	900	(Shares)	
Amalgamation Reserve	9000	Bank	100
	10100		10100



Demerger - Definition



- Section 2(19AA)
- Pursuant to Section 391 to 394 of Companies Act 1956
- 'undertaking' transferred as a 'going concern'
- all 'property' of and all 'liabilities' relating to the undertaking transferred at 'book values'
- shares issued as consideration to shareholders of transferor co on a proportionate basis
- shareholders hold at least 3/4th in value of shares of transferee co (other than already holding)
- Transfer has to be at book value without revaluation of assets
- Above conditions are cumulative



CASE STUDY ON DEMERGER PROIR TO CONVERSION IN TO LLP

This Option can be considered in case of CASH RICH Corporate to hive off Investment Division and LLP
 Balance Sheet of A Pvt. Ltd (With Sales Exceeding Rs.60 Lacs for last 3 yrs)

Liability	BUSINESS	INVEST	Assets	BUSINESS	INVEST
Share Capital	500	500	Investments	5000	
Reserve	4500	5500	STOCK		6000
Total	5000	6000	Total	5000	6000

Balance Sheet of B Pvt. Ltd (With Sales Less Than Rs.60 Lacs for Last 3 Yrs)

Liability	Amount	Assets	Amount
Share Capital		Investments	100
Reserve			
Total		Total	100



DEMERGED INVESTMENT DIVISION IN TO B LTD AND RETAIN BUSINESS IN A LTD

Resultant Balance Sheet (Post DEMERGER) will be

Balance Sheet of B Pvt. Ltd (With Sales Less Than Rs.60 Lacs for Last 3 Yrs)

Liability	Amount	Assets	Amount
Share Capital	5100	Investments	5100
Reserve	0		
Total	5100	Total	5100

NOW B PVT LTD can be Converted in to LLP & A LTD CAN DO EXISTING BUSINESS



Major Cost With Merger/Demerger



- Stamp Duty
 - Higher of
 - a) 5% of Market Value of immovable property located in Maharashtra OR
 - b) 0.7% of the market value of shares allotted in exchange and consideration.

- ROC Filing Fees
 - a) Stamp duty for increasing AOA = 0.2%
 - b) For increasing Authorized Capital = 0.5% (above Rs.1Cr.)

Total 0.7%

Stamp duty Mitigation

Current Scenario

A Ltd. Balance Sheet

Particulars	Amt	Particulars	Amt
Sh Cap	100	Fixed Asset	5000
Reserve	900	Other current asset	6000
Other liabilities	10000		
	11000		11000

B Ltd. Balance Sheet

Particulars	Amt	Particulars	Amt
Sh Cap	50	Fixed Asset	6000
Reserve	500	(property)	
Other liabilities	7000	Other current asset	1550
	7550		7550



Stamp duty/ROC -Existing Scenario

Now,

If B Ltd Merged With A Ltd.

Then,

Stamp duty will be

HIGHER Of

a) 5% of property 300

b) 0.7% of Consideration 3.85

(Consideration=net worth)

Applicable Stamp duty option a 300

Now,

If B Ltd Merged With A Ltd.

Then,

ROC Fees will be

a) 0.5% of Additional Shares to be issued 2.75

(Addl Shares = net worth)

and

b) 0.2% of Additional Shares to be issued 1.1

(Addl Shares = net worth)

Applicable Cost (ROC) 3.85



Alternate Scenario

Make Target Company (B Ltd) as Subsidiary Company

A Ltd. Balance Sheet (Bef Amalgamation)



Particulars	Amt	Particulars	Amt
Sh Cap	100	Fixed Asset	5000
Reserve	900	Investment in B Ltd	550
Other liabilities	10000	Other current asset	5450
	11000		11000

B Ltd. Balance Sheet(Bef Amalgamation)

Particulars	Amt	Particulars	Amt
Sh Cap	50	Fixed Asset	6000
Reserve	500	(property)	
Other liabilities	7000	Other current asset	1550
	7550		7550

A Ltd (Post Amalgamation)

Particulars	Amt	Particulars	Amt
Sh Cap	100	Fixed Asset	11000
Reserve	900	Other current asset	7000
Other liabilities	17000		
	18000		18000

Applicable Stamp Duty will be NIL (As there will be Cancellation of Shares of B Ltd)



Roc Mitigation

- Swap ratio should be structured in such a way that acquirer company will issue shares at premium.
- For that acquire company share valuation either on DCF or NAV whichever is applicable should be higher
- This will Result into Lesser Issue of shares due to amalgamation/Demerger Resulting into lesser Roc fees for increasing Authorized capital



CA Divyesh V Mehta
Partner

