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Resulting company entitled to pro-rata/proportionate TDS, advance-tax and MAT credit post demerger

Background

Recently, the Ahmedabad Bench of Income-tax Appellate Tribunal (the Tribunal) in the case of Adani Gas Limited[1] held that credit of Tax Deducted at Source (TDS), Minimum Alternate Tax (MAT) and advance tax paid by the demerged company (relatable to the demerged undertaking) is allowable in the hands of the resulting company upon demerger.

The Tribunal held that the scheme of arrangement provided for the transfer of all assets and properties of the demerged undertaking to the resulting company and hence would include the transfer of various tax credits. Further, relying on the Supreme Court's decision in the case of Marshall & Sons[2] the Tribunal held that the tax credits should be available to the resulting company with effect from the appointed date.

Facts of the case

- Pursuant to the Scheme of demerger approved by the Gujarat High Court, the gas distribution division (demerged undertaking) of Adani Energy Limited (demerged company) was demerged to Adani Gas Limited (the taxpayer or resulting company). The appointed date for the demerger was 1 January 2007, and the same was approved vide High Court order dated 19 November 2009.
- Post completion of the demerger, the demerged company and the taxpayer revised their return of income and the taxpayer, while filing its return of income, claimed the pro-rata credit of TDS, MAT and advance tax paid by the demerged company. However, the Assessing Officer (AO) rejected the claim of the taxpayer.
- The Commissioner of Income-tax (Appeals) [CIT(A)] while upholding the order of the AO held that the entire tax credit shall be available in hands of the demerged company only since the demerger scheme did not contain any provision with respect to bifurcation of the various tax credits between the demerged company and the resulting company.

Taxpayer's contentions

- The entire demerger exercise is to be tax neutral and hence both the companies should be given credit for taxes paid on total income of the respective companies such that the total refund claimed by the companies is not less than the refund claimed as per the original return of income.
- The taxpayer further submitted that since the taxes resulted mainly from activities pertaining to the gas distribution division, they should be allowable in hands of the taxpayer on a proportionate basis.

[1] Adani Gas Limited v. ACIT (ITA Nos. 2241 & 2516/Ahd/2011) – Taxsutra.com
[2] Marshall Sons & Company India Ltd v. ITO [1997] 223 ITR 809 (SC)

- Further in terms of the provisions of Section 199 and Section 200 of the Income-tax Act, 1961, the taxpayer contended that as long as the tax deducted at source has been paid over to the government and the certificates in respect of the same have been issued by the tax deductor, the AO should grant due credit of TDS (paid by the demerged company) to the taxpayer on the basis of original TDS certificates produced before him/her.

Tribunal's ruling

- Referring to the definition of the term 'demerger' under Section 2(19AA) of the Income-tax Act, 1961, the Tribunal observed that a demerger involved the transfer of all properties of the demerged undertaking to the resulting company. Accordingly since the scheme of demerger provided for the transfer of all assets of the demerged undertaking along with all possible benefits including deferred tax benefits; tax credits should be permissible in the hands of the taxpayer.

- The Tribunal relied on the Supreme Court's decision in the case of Marshall Sons & Company wherein it was held that the date of amalgamation/transfer is the date specified in the demerger scheme as 'the transfer date' as approved by the court. The Tribunal accordingly held that once the demerged undertaking ceases to exist with effect from the appointed date as mentioned in the demerger scheme, the MAT credits, TDS and advance tax credits of the demerged undertaking are entitled to be considered in the hands of the resulting company on a pro-rata basis since the demerged company is deemed to have carried out its business from the appointed date on behalf of the resulting company.

- In drawing the above conclusion, the Tribunal also drew support from the judgment of Torrent Private Limited[3] and Cadila Healthcare Ltd[4]. In case of Torrent Private Limited, the dividend distribution tax paid by the petitioner company was held to be refundable from appointed date of the scheme came into effect, the petitioner no longer existed by virtue of its merger with the parent company and hence, there cannot be payment of dividend during that period by the parent company to its own self.

- In the ruling of Cadila Healthcare Limited, it was held that sales undertaken between transferor company and transferee company between the appointed date and effective date of scheme of amalgamation cannot be regarded as sales between two independent entities but would be treated as branch transfers and hence the sales tax paid on sales during the interim period are liable to be refunded to the taxpayer.

- Accordingly the Tribunal concluded that once the demerged gas distribution undertaking ceased to exist with effect from 1 January 2007 being the appointed date of the demerger scheme, the taxpayer (resulting company) should be entitled to various pro-rata TDS, advance tax and MAT credits.

Our comments

The issue of claim of tax credits with effect from the appointed date by the amalgamated company/resulting company in a scheme of arrangement has been a matter of litigation at lower levels in the absence of any specific provisions allowing such claims. In delivering its ruling, the Tribunal has gone beyond the technical and literal reading of the provisions of the law and has adopted a more liberal and logical approach to provide tax neutrality to such schemes in accordance with the spirit of law. It may be pertinent to mention that Mumbai ITAT has also in the past (in the case of SKOL Breweries Ltd v. ACIT) allowed the transfer of MAT credit in case of a merger; treating it as an asset of the amalgamating company.

The Tribunal's decision on availability of proportionate tax and MAT credit in case of a demerger is a welcome one and is expected to go a long way in providing greater certainty to taxpayers while undertaking such court approved restructuring schemes.

[3] Torrent (P) Ltd v. CIT [2013] 217 Taxman 149 (Guj)
[4] Cadila Healthcare Ltd (Special Civil Application No.9980 of 2001, 13/16 July 2012)

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