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NEWSLETTER

PUNE BRANCH OF WIRC OF ICAI

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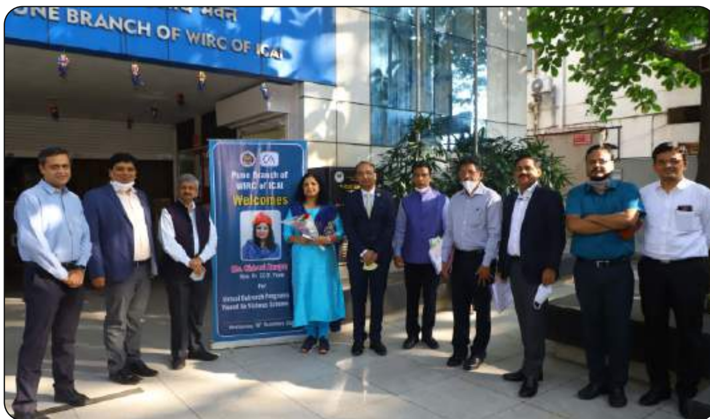
PUNE BRANCH OF WIRC OF ICAI

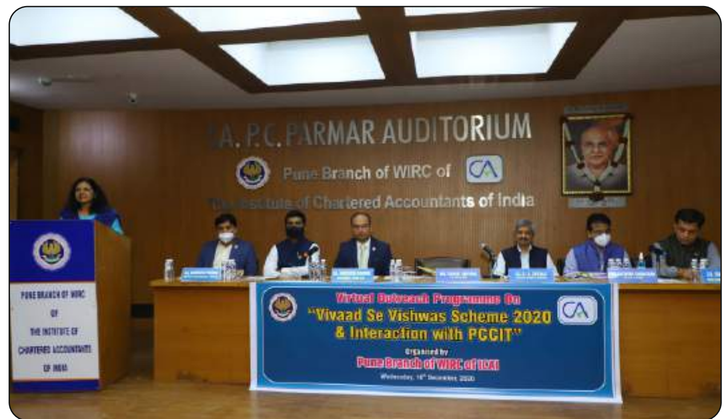
List of Recorded Prgorammes held in the Month of December 2020 Available on Pune ICAI YouTube Channel

SR. NO.	DATE	TOPIC	SPEAKER	LINK
1	16th December, 2020	Outreach Programme & Interaction with Pr. CCIT on Vivaad Se Vishwas Scheme 2020 (Virtual)	Ms. Chhavi Anupam, Pr. CCIT, Pune	https://youtu.be/_Q1zNDPVXFw
2	20th December, 2020	Virtual CPE Meeting on "e-Invoicing and Recent Changes in GST Return System & Other Procedures"	CA Anupama Agaarwal & CA Yogesh Ingale	https://youtu.be/A_0mT2_KAxE
3	24th December, 2020	Memorandum of Understanding (MoU) Signing Ceremony between Savitribai Phule Pune University (SPPU) and The Institute of Chartered Accountants of India (ICAI)	Signing Ceremony	https://youtu.be/BsBmSPJ68eI

Outreach Programme & Interaction with Pr. CCIT on Vivaad Se Vishwas Scheme 2020

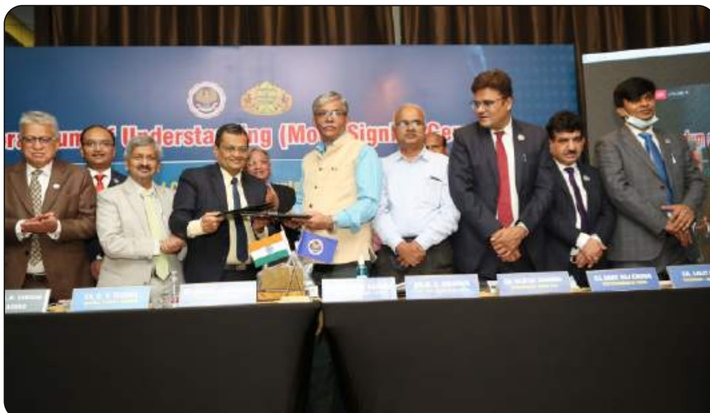


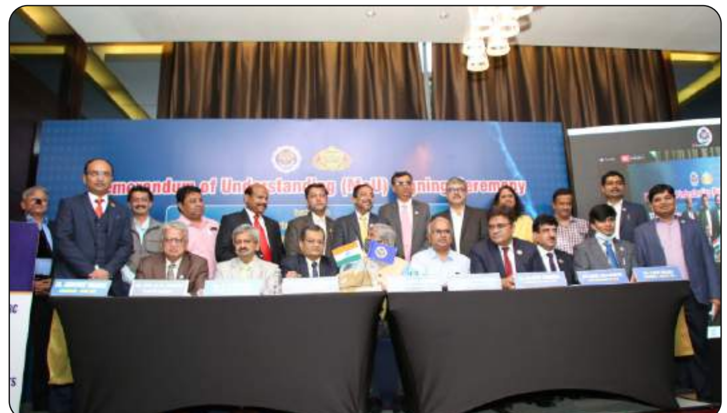
Ms. Chhavi Anupam, Pr. CCIT, Pune & Officials of CCIT, Pune with MCM of Pune ICAI



Ms. Chhavi Anupam, Pr. CCIT, Pune & Officials of CCIT, Pune with MCM of Pune ICAI

Memorandum of Understanding (MoU) Signing Ceremony between Savitribai Phule Pune University (SPPU) and The Institute of Chartered Accountants of India (ICAI)





All Aspects of Conversion of Company into LLP

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Introduction

Limited Liability Partnerships (LLP) are emerging as a popular business structure for their multiple advantages. It is simpler yet corporate form of business where in all good features of both Company and Partnership firm are present. It is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.

The LLP is a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP. The LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name. Further, no partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct. Since LLP contains elements of both 'a corporate structure' as well as 'a partnership firm structure' LLP is called a hybrid between a company and a partnership.

The LLP structure is available in countries like United Kingdom, United States of America, various Gulf countries, Australia and Singapore. On the advice of experts who have studied LLP legislations in various countries, the LLP Act is broadly based on UK LLP Act 2000 and Singapore LLP Act 2005. Both these Acts allow creation of LLPs in a body corporate form i.e. as a separate legal entity, separate from its partners/members.

Advantages of LLP

- LLP can be formed by any amount of capital. There is no need for minimum capital for LLP.
- It requires a minimum of 2 partners and there is no limit on the maximum number of partners of the LLP.
- The cost of registering LLP is low as compared to a company.
- All limited companies have to get their accounts audited but in case of LLP there is no audit requirement unless the contributions of LLP exceeds Rs. 25 lakh or annual turnover exceeds Rs. 40 lakh.
- The LLP has very limited compliances as compared to the Company. It has to file yearly income tax return and two documents with the RoC i.e. annual return and statement of accounts and solvency.
- LLP is treated in par with the partnership firm. The provision of dividend distribution tax is not applicable on LLP. Also under Section 40(b) deductions are allowed on the interest given to partners, any payment of salary bonus commission or remuneration.

What is the need of Conversion from Private Company into LLP?

- LLP will have more flexibility as compared to a company.
- LLP will have lesser compliance requirements as compared to a company.
- LLP does not have to have its accounts audited if the annual turnover of the LLP is less than Rs. 40 lakhs and the capital contribution is less than Rs. 25 lakhs.
- A dividend received from Company is taxable in the hands of shareholders as per their applicable slab rate. While taxation structure for LLP is simpler. LLP is subjected only to Income tax. Dividend Distribution is not applicable on LLP. Once profit is declared and tax is paid by LLP, the distributed income is tax free in the hands of the partners.
- A paying back the capital i.e Buy back is very complex and costly exercise in case of company. However, in LLP, partners can withdraw his/her capital at any point of time by writing a simple letter. There is no tax implications on withdrawal of capital from LLP.

- There is no stamp duty on all movable and immovable properties of the company; on conversion of a private limited company into LLP as such properties automatically vest in the LLP. No instrument required to be executed and hence no stamp duty is required to be paid.

- No Capital gain tax shall be charged on transfer of property from the company to LLP, if the conditions stipulated in the Section 47(xiiib) of the Income Tax Act 1961, are fulfilled.

- Carry forward and set off losses and unabsorbed depreciation of the company is deemed to be loss/depreciation of successor LLP the previous year in which conversion was effected, thus such loss can be carried for further 8 years in the hands of the successor LLP.

Legal Framework for Conversion

Section 56, Third Schedule and Fourth Schedule of LLP Act- 2008

A Private Limited Company or Unlisted Public Company may convert into a Limited Liability Partnership in accordance with the provisions of Section 56 and the Third and Fourth Schedule of LLP Act, 2008.

Eligibility of Conversion

- There is no security interest in its assets subsisting or in force at the time of application; and
- The partners of the limited liability partnership to which it converts comprise all the shareholders of the company and no one else.

Requirements for conversion of company into LLP

- Every member of the company must agree with the decision of conversion.
- All the members become the partners of an LLP and no one else.
- The latest copy of Income tax return is to be filed with ROC.
- Not just the members, all the creditors of the company must also agree with the conversion.
- Under Companies Act, no prosecution should have been initiated procedure to be followed.
- No open (unsatisfied) charges should be pending against the company.
- At least one balance sheet and annual return should have been filed by the company after its incorporation.
- The company should be having share capital.
- The company should not be a Section 25 company/Section 8 Company under Companies Act, 1956/2013.

Process for Conversion of Company into LLP

- Call for Board Meeting and pass Board Resolution for the conversion of the company into LLP.
- Take the Written consent of all the shareholders for conversion of Company into LLP.
- File application for name availability in web based form 'RUN-LLP' with the RoC. Attach the Board Resolution and proposed object clause with the name availability application.
- Once the name is approved, execute all necessary documents like consent, subscriber sheet etc. and file form FiLLip and form 18 with the RoC.

Attachments of form FiLLip

- Subscriber Sheet
- Consent of Designated Partner
- Proof of Address of Registered office of LLP i.e Sale Deed / Lease Deed / Rent Agreement
- NOC of owner of registered office, if taken on rent / lease.
- Latest Utility bill of registered office
- Detail of LLP(s) and/ or Company(s) in which partner/ designated partner is a director/ partner

Attachments of form 18

- Statement of shareholders. It is the document given by each shareholders giving their consent and statement.
- Statement of Assets and Liabilities of the company duly certified as true and correct by the auditor.
- List of all the secured creditors, if any along with their consent to the conversion.
- Copy of acknowledgement of latest income tax return.

➢ Once conversion is approved by the RoC execute LLP Agreement and file the same with the RoC in e-form LLP 3 within 30 days of approval of conversion by RoC.

Capital Gain on transfer of Assets and Liabilities

The finance Act, 2010 has inserted a new Clause (xiiib) in section 47 and a new sub-section (4) in section 47A of the Act with effect from assessment year 2011-12. If the following conditions are satisfied then the transfer of capital asset or intangible asset to LLP or any transfer of share or shares held in Company by a shareholder on conversion of Company into LLP shall not be regarded as transfer:

➢ all the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership;

➢ all the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;

➢ the shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership;

➢ the aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than fifty per cent at any time during the period of five years from the date of conversion;

➢ the total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed sixty lakh rupees;

➢ the total value of the assets as appearing in the books of account of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed five crore rupees; and

➢ no amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.

If all the above conditions are complied with, the conversion shall not attract capital gains tax either for the Company or the Successor LLP or for the shareholders of the Company, who became partner in the successor LLP and get share of profits and capital in the LLP in lieu of their shares in the Company.

If any of the above conditions are not complied with, then as per provisions of Section 47A(4) such transfer of Capital Assets & Intangible assets deemed to be liable to Capital gains of the successor LLP or the Shareholders of the predecessor Company in the previous year in which such non-compliance took place.

What if Predecessor Company does not have any capital assets and intangible assets?

Transfer as per Income Tax includes disposing of or parting with an asset or any interest therein or creating any interest in any asset in any manner whatsoever. Even if there is no capital assets and intangible assets in a Predecessor Company, there is conversion of the equity shares into partnership interest in an LLP and hence this

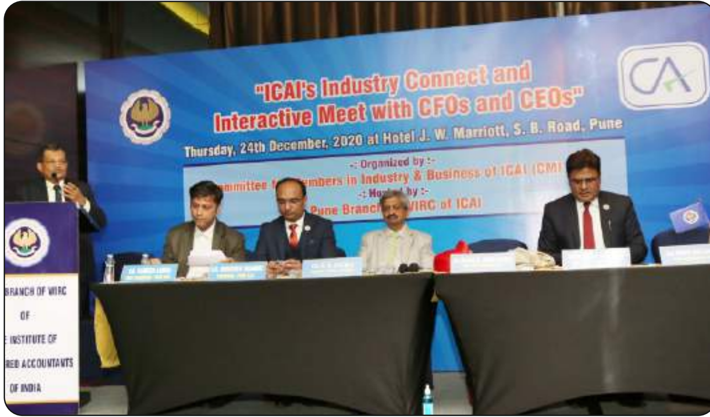
transaction is clearly covered within the definition of transfer. So, Even if there is no transfer of immovable property, LLP has to follow the above mentioned conditions otherwise respective shareholders have to pay capital gain tax on the difference between the values of their interest in LLP less cost of acquisition of shares in erstwhile LLP.

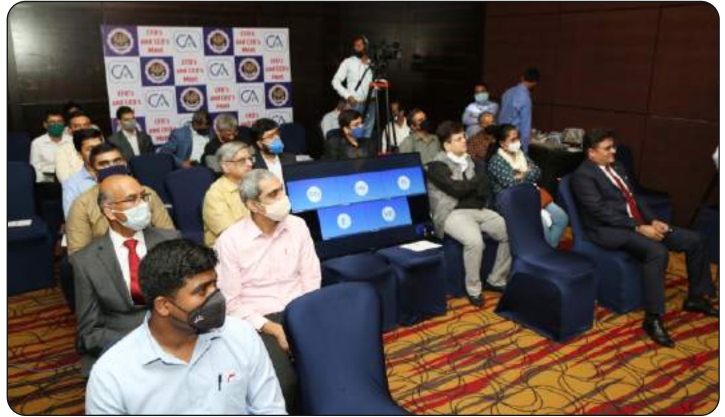
(Advance ruling in the matter of Domino Printing Services PLC)

Conclusion

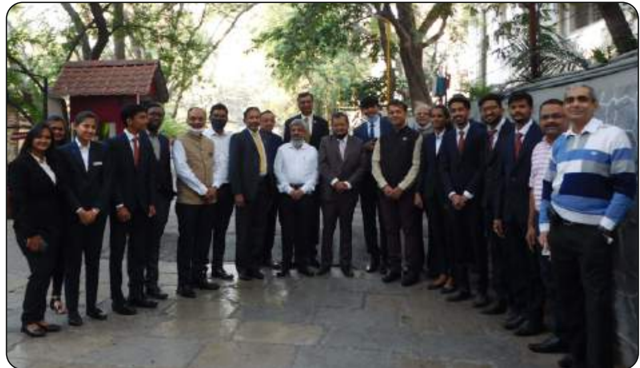
Owing to flexibility in its structure, compliances, tax and operation, LLP would be useful for small and medium enterprises, in general. Internationally, LLPs are the preferred vehicle of business, particularly for service industry or for activities involving professionals. The conversion from the existing corporate structure can be made to a LLP while retaining the advantages of Limited Liability and less compliances.

ICAI's Industry Connect and Interactive Meet with CFOs and CEOs





Interactive Meeting with Hon. Vice president of ICAI



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Goodwill – Not in Good Faith Anymore?

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Renowned American Entrepreneur and Pioneer in Departmental Store Business – Late Marshall Field once quoted "Goodwill is the only asset that competition cannot undersell or destroy".

The quote is literally true in its own sense. Goodwill is supposed to be the brand value that the business or organisation has created over a period. Yet, it is considered to be inappropriate to recognise the goodwill on its own by the business enterprise. Goodwill is defined to be an intangible asset that is associated with the purchase of a company or a set of assets of the company by another company. In a general sense, goodwill is the excess price paid by the acquirer company as compared to the net asset fair value purchased in the acquisition after considering all assets and liabilities acquired in the process. Goodwill is represented by characteristics like the brand value of the company, its loyal customer base, its human resources strength, technical know-how built by the company and the market presence it has created.

Accounting Perspective

As Goodwill is an intangible asset, recognition of the goodwill in the books of account is practically difficult unless the goodwill is acquired as a part of business combination. Self-generated Goodwill cannot be recognised in the books of account as it is not possible to apportion a fixed amount to it which would reflect its true and fair value. The treatment of goodwill depends upon the accounting policies and standards followed by the company.

As per the provisions of Accounting Standard – 14 "Accounting for Amalgamation", goodwill acquired on merger has to be recognised as an asset and amortised on a systematic basis over the useful life of the asset. Considering the nature of the goodwill, it is difficult to ascertain the useful life with reasonable certainty. As such, it is a general practice to amortise the same over a period of 5 years.

Ind-AS 103 "Business Combinations" suggests that acquirer needs to calculate the goodwill to be recognised in the books based on the fair value of the net assets acquired as on the acquisition date. Furthermore, such goodwill is required to be tested for impairment every year as per the provisions of Ind-AS 36 "Impairment of Assets".

It is pertinent to note that under either of the account standards, the two highlighted parts are initial recognition of acquired goodwill and secondly the amortization over the useful life. But the most crucial part is that the Goodwill is recognised as an Asset, which is nothing but a resource; future economic benefits of which are supposed to flow to the entity.

Tax Perspective

Whether to treat goodwill as an asset has always been a debatable issue under the Income-tax Act, 1961 ('the Act' or 'ITA'). Under the provisions of the Act, an assessee is allowed depreciation on the assets employed for the purpose of the business. Few important provisions revolving around the depreciation are section 2(11), section 32 and section 43(1).

Explanation 3 to section 32(1) defines an asset to include tangible assets like building, machinery, plant, furniture and intangible assets like know-how, patents, copyrights, trademarks, licenses or any other business or commercial rights of similar nature. Similar wordings are used in the definition of block of assets under section 2(11) of the Act.

The whole dispute revolved around the fact that Goodwill has no where been mentioned as an asset under either of the provisions of the Act. Furthermore, it may not be justifiable to compare 'other business or commercial rights of similar nature' with the nature of the goodwill. Accordingly, the tax authorities have always been of the view that Goodwill does not amount to an asset and accordingly, charge of depreciation on goodwill may not be allowed under section 32 of the Act.

In a landmark judgement, Hon. Supreme Court in the case of Smiff Securities Limited [(2012)348 ITR 302 (SC)], it was deduced that Goodwill forms part of the assets of a business or a profession and accordingly it was entitled for claiming depreciation under section 32 of the Act. This prompted companies recognising Goodwill in their books arising out of business restructuring transactions and claiming depreciation @ 25% which is the rate adopted for providing depreciation on Intangible Assets.

The twist in the story came with the amendments brought in by the Finance Bill, 2021. The Government has proposed amendment to section 2(11) to provide that 'block of assets' shall not include Goodwill. Furthermore, section 32(1)(ii) was amended to provide that Goodwill shall not be considered to be an asset and therefore shall not be eligible for depreciation. Corresponding amendments were proposed to section 50, 55 and 49(1) of the Act in order to rationalise calculation of Capital Gains on Goodwill.

While proposing the aforementioned amendments, the Government put forth a justification that the calculation of depreciation under section 32 is done after considering provisions of section 43(6)(c) and section 43(1). Section 43(1) defines Actual Cost as actual cost of an asset to the assessee. Explanation 7 to section 43(1) points out that actual cost of capital asset transferred in a transaction of amalgamation in the hands of the amalgamated company shall be the same as that of the amalgamating company as if the transaction of amalgamation has not taken place. Furthermore, explanation 2 to section 43(6) specifically states that the actual cost of the block of assets in the hands of amalgamated company would be the written down value of that block in the hands of the amalgamating company in the immediately preceding previous year as reduced by the depreciation actually allowed in that immediately preceding previous year. The Memorandum explaining the finance bill also contended that if these provisions are applied, there could be no depreciable goodwill in some of the business reorganisation cases. It was also observed that in some cases, there could be a valid claim of depreciation on the goodwill where it has been acquired by was of a purchase transaction. However, it was contended that there might be a situation where goodwill may not undergo any depreciation at all considering the fact that the appreciation or depreciation would depend upon how the business runs.

Accordingly, the Finance Bill, 2021 proposed the aforementioned amendments thereby restricting the claim of depreciation on goodwill with effect from April 01, 2021; applicable to the Assessment Year 2021-22 and subsequent assessment years.

Way Forward

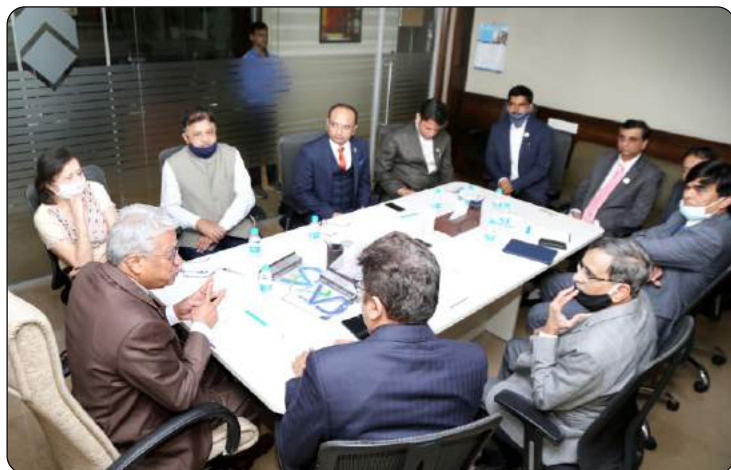
The proposed amendment is expected to have a long-lasting impact on the Mergers and Acquisition transactions. Some scholars are even believing these provisions to be draconian which would kill the spirit of a negotiation in a given transaction. Companies now will impel to consider biased Purchase Price Allocation; thereby refusing to recognise goodwill in the books of account.

It is still uncertain if the department is going to suggest a treatment for goodwill already recognised in the books of account as a result of transaction which has taken place before the introduction of the aforesaid amendments. It is believed that the companies will either be forced to consider full impairment in the financial year 2020-21 itself and take a write-off in the books or the government will prescribe a method of impairment in line with the provisions of Ind-AS 36.

Non-allowance of depreciation on Goodwill under the Income Tax will result into tougher negotiations in a given M&A transaction. From buyer's perspective, it will result into higher cash outflows on account of tax expenditure. Accordingly, buyer will demand revised valuations and seek more bargain in the expected consideration.

This hardship has certainly led to an important question in the M&A industry – Goodwill; not in good faith anymore???

Interactive Meet with Officials of Cosmos Co-operative Bank

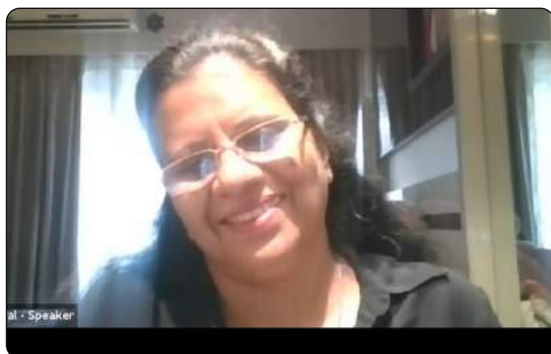


Seminar on "Key Updates related to GST Return and GST Audit"

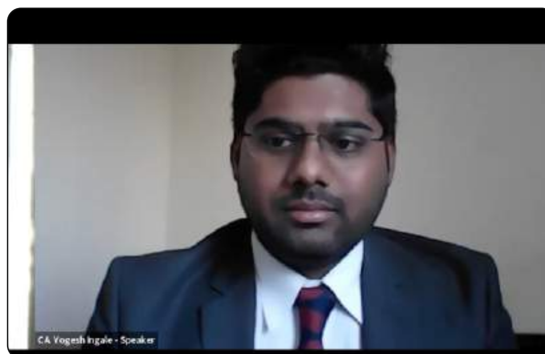
CA. Vaishali Kharde, Speaker

Participants

VCM on "e-Invoicing and Recent Changes in GST Return System & Other Procedures"

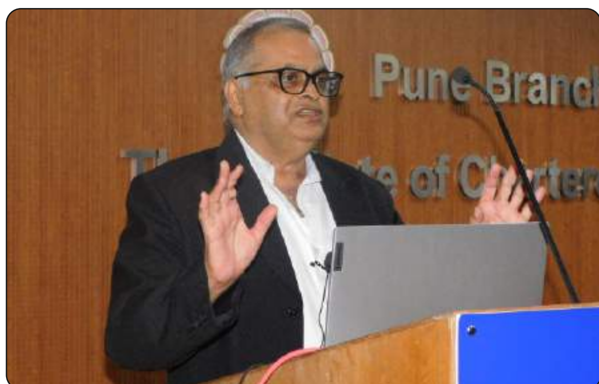


CA. Anupama Agarwal, Speaker



CA. Yogesh Ingale, Speaker

Lecture Meet on "Issues in Tax Audit"



CA. Sharad Shah, Speaker

Participants

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