
SLUMP SALES UNDER INDIAN LAW: TAX EFFICIENCY OR REGULATORY GREY ZONE

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ABSTRACT

This article critically examines the legal and tax framework governing slump sales in India, a method of business transfer wherein an undertaking is sold as a going concern for a lump-sum consideration without assigning individual values to assets and liabilities. While slump sales offer significant tax advantages and operational efficiency, they occupy a regulatory grey zone due to the difficulty in distinguishing them from structured asset sales designed to exploit preferential tax treatment. The article explores statutory provisions under the Income-tax Act, 1961, including recent amendments post the *Areva T&D* ruling, and highlights key judicial pronouncements that have shaped the understanding of “undertaking” and “going concern.” It further analyzes issues arising from consideration structuring, exclusion of liabilities or employees, and the treatment of non-compete fees and goodwill. The discussion underscores the challenges posed by inconsistent interpretations and the reliance on judicial discretion, which creates uncertainty for businesses seeking compliant structuring. Ultimately, it advocates for clearer legislative guidance to ensure transparency and reduce litigation in the context of such transfers.

I. Introduction: The Evolving Landscape of Business Transfers in India

Slump sale is a method of restructuring wherein a business is transferred as a “going concern” for a consideration which is in lump sum without delineating or classifying individual assets within the business or determining its valuation.¹ A slump sale is different from an asset purchase as in an asset purchase, specific assets are valued and then transferred whereas in a slump sale the entire business is transferred as a going concern. Acquirers in an asset purchases get to select assets and avoid historical liabilities, but this often has tax disadvantages for sellers.² As a middle ground, “business transfer” or “slump sale” has become increasingly popular due to its growing advantages.³ This article will analyze how the existing tax and regulatory framework in India governs the procedure of slump sale and whether it sufficiently distinguishes between genuine business transfers structured as slump sales and transactions that might be disguised asset sales to avail preferential tax treatment, exploring the ambiguities and challenges therein.

II. Defining Slump Sale: Legal and Tax Foundations

In the Indian context, “business transfer” and “slump sale” are used interchangeably, referring to the transfer and sale of an entire business undertaking on a going concern basis for a lump-sum consideration.⁴ “Slump sale” is primarily a tax concept defined under Section 2(42C) of the Income-tax Act, 1961 (ITA) as the “transfer of one or more undertakings, by any means, for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales”.⁵

However, in the *Areva T&D India Ltd. v. Commissioner of Income Tax* case, where the key issue was whether the transfer of an undertaking by Areva to its subsidiary in consideration for equity shares counted as a “sale” under Sec 50B of the Income Tax Act, the court ruled that since the transfer was for non-monetary consideration it does not constitute as a sale and so it will not be considered as a slump sale.⁶

To counter this ambiguity The Finance Act, 2021, amended the definition of 'slump sale' to

¹ V. K. Subramani, *Opinion: Slump Sale V. Demerger*, Taxmann (Dec. 20, 2021).

² Bharucha & Partners, *Can A Slump Sale Carve-Out Certain Assets And Liabilities?*, Mondaq (Feb. 3, 2023).

³ Ipsita Agarwalla et al., *Business Transfer Why, how and when?*, Nishith Desai Associates.

⁴ *Id.*

⁵ *Id.*

⁶ *Areva T&D India Ltd. v. Commissioner of Income Tax* (2020) 428 ITR 1.

include transfers "by any means," so as to widen its scope beyond the traditional understanding of 'sale' and overturning such judicial decisions like that of Areva T&D Ltd, that excluded transfers in exchange for non-monetary consideration like shares. Prior to this amendment, there was debate on whether consideration in kind would qualify as a sale.⁷

Another requirement for a slump sale is that the subject matter must be one or more undertakings of the seller. Explanation 1 to Section 2(19AA) defines an "undertaking" to include "any part of an undertaking or a unit or a division of an undertaking or a business activity taken as a whole but does not include individual assets or liabilities or any combination thereof not constituting a business activity".⁸The transferred undertaking should be an identifiable stand-alone business activity which will also include all its assets, liabilities, employees, contracts, and licenses which are required for independent operation and revenue generation of that undertaking.⁹

Furthermore, the most essential requirement is for the transfer to be a "going concern", which refers to that there should be no break or cessation in the operations of the transferred undertaking. The transfer should be simultaneous, ensuring the buyer can immediately run the business.¹⁰ Indian courts emphasize that the undertaking must be capable of independent operation by the purchaser. Indian Courts have held and established that the undertaking being sold includes "the entirety of the business irrespective of separate ingredients" and is not dependent on other for its operations.¹¹

Another requirement for a slump sale is that the consideration must be a single amount without assigning individual values to assets and liabilities, as the buyer is acquiring the business as a whole.¹² However, valuing assets for stamp duty or registration fees does not negate the lump-sum nature.¹³

III. Tax and Regulatory Implications Favoring Slump Sales

A significant advantage of a slump sale over an asset sale is its tax treatment for the seller. If

⁷ V. K. Subramani, *Opinion: Slump Sale V. Demerger*, Taxmann (Dec. 20, 2021).

⁸ The Income Tax Act, 1961 § 2(19aa).

⁹ Ipsita Agarwalla et al., *Business Transfer Why, how and when?*, Nishith Desai Associates.

¹⁰ *Id.*

¹¹ Bharucha & Partners, *Can A Slump Sale Carve-Out Certain Assets And Liabilities?*, Mondaq (Feb. 3, 2023).

¹² Stephanie Fogel et al., *India: Does your transaction qualify as a slump sale?*, DLA Piper (Aug. 17, 2022).

¹³ Bharucha & Partners, *Can A Slump Sale Carve-Out Certain Assets And Liabilities?*, Mondaq (Feb. 3, 2023).

the undertaking has been held for more than 36 months, it is deemed a long-term capital asset, and the entire profits or gains are subject to long-term capital gains tax at 20%. If held for not more than 36 months, it's subject to short-term capital gains tax at 30% for domestic companies and 40% for foreign companies. For computing capital gains, the net worth of the undertaking is considered the cost of acquisition.¹⁴

Under Section 50B of the Income Tax Act, the Cost Of Acquisition of a transferred undertaking is its net worth, without indexation. Net worth is the aggregate value of total assets which includes depreciable assets at written down value, certain assets at nil, and others at book value reduced by liabilities from the books of account. A chartered accountant's report in Form 3CEA is required to certify net worth computation.¹⁵ Moreover, Slump sale are exempt from GST as well.

Additionally, Section 180 of the Companies Act, 2013 requires an Indian public company selling whole or substantially the whole of its undertaking to seek the prior consent of the shareholders by way of a special resolution.¹⁶ Requires approval from the boards of directors of both buyer and seller. Public companies selling substantially their whole undertaking also need prior shareholder consent via a special resolution (75% approval) if the undertaking meets certain investment or income thresholds.¹⁷

If the business transfer qualifies as a 'combination' under the Competition Act, 2002, it requires prior consent from the Competition Commission of India (CCI) if certain financial thresholds based on assets and turnover of parties and the acquirer group are met.¹⁸ There have also been recent amendment this amendment states that any transaction involving the acquisition of control, shares, voting rights, or assets of an enterprise, or a merger or amalgamation, where the deal value exceeds INR 2,000 crore, will require approval from the Competition Commission of India if the enterprise being acquired or merged has 'substantial business operations in India'.¹⁹

¹⁴ Ipsita Agarwalla et al., *Business Transfer Why, how and when?*, Nishith Desai Associates.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

IV. Inadequate Distinctions: Genuine Transfer vs. Disguised Asset Sale

There are certain ambiguities in demarcating genuine business transfers from disguised asset sales, primarily due to the flexibility allowed and the inherent complexities of commercial transactions.

While a slump sale ideally involves the transfer of all assets and liabilities necessary for conducting the business there are case laws that indicate that exclusion of certain assets and liabilities is permitted as long as the transferred assets and liabilities are sufficient for conducting the business and generating sustainable revenue on a stand-alone basis.²⁰

For instance, in the *Rohan Software Private Limited v. Income Tax Officer* case, The ITAT Mumbai held that the exclusion of certain non-essential assets from the transfer does not defeat the characterization of a transaction as a slump sale, provided the core of the business is transferred in such a manner that the business remains operational as a whole under the new owner.²¹

Furthermore, there is also clarity by the Delhi High Court in *Triune Projects Private Limited v. Deputy Commissioner of Income Tax* where it was held that the exclusion of certain defunct assets and bad debts will not affect the slump sale nature of a business transfer.²²

To make it further clear the courts have also held that exclusion of all liabilities generally means the transfer will not qualify as a slump sale. Similarly, excluding all or a sizeable number of employees can lead to the transfer not being considered a going concern, and thus not a slump sale.²³ Furthermore, In June 2020, the Mumbai Bench of Income Tax Appellate Tribunal in the case of *M/s. Archroma India Pvt. Ltd. v. ITO* it was further clarified that transfer of business by way of slump sale falls within the ambit of Section 170 of the Act and constitutes succession of business by the transferee and Section 170 of the Act states that where a predecessor carrying on any business is succeeded by the successor, who subsequently continues to carry on that business.²⁴

²⁰ Stephanie Fogel et al., *India: Does your transaction qualify as a slump sale?*, DLA Piper (Aug. 17, 2022).

²¹ *Rohan Software Private Limited v. Income Tax Officer* (2008) 304 ITR 314 (Mumbai).

²² Bharucha & Partners, *Can A Slump Sale Carve-Out Certain Assets And Liabilities?*, Mondaq (Feb. 3, 2023).

²³ Sumit Bansal et al., *Smooth Transitions: Navigating Succession in Business Transfers on Slump Sale Basis*, S&R Associates (July 11, 2024).

²⁴ *Id.*

Nuances in Lump-Sum Consideration and Valuation:

While consideration must be paid lump-sum, working capital adjustments and deferred payments or earn-outs are commercially accepted and generally do not change the nature of a slump sale, as has also been clarified by specific rulings.²⁵ The Finance Act, 2021, clarified that the "full value of consideration" (FVC) for slump sales is the fair market value (FMV) of the undertaking as determined by prescribed rules, with the higher of book value-based formula or actual consideration being considered.²⁶

An area of debate and potential mischaracterization arises when the excess paid over the book value of assets is debated between goodwill and non-compete fees. The buyer might prefer to allocate part of the consideration to non-compete fees, potentially claiming it as a revenue expense or an intangible right eligible for amortization.²⁷ Depreciation on goodwill is generally not allowed for tax purposes since the Finance Act, 2021.²⁸ The seller on the other hand prefers the entire consideration to be treated as a capital receipt to avail beneficial long-term capital gains tax treatment. If non-compete fees are treated as income under Section 28(va) of the ITA, they are taxed as business income at a higher rate unless they form an integral part of the business/asset transfer.²⁹

These conflicting tax objectives lead to heavy negotiation in slump sale agreements. While Section 28(va) aims to tax non-compete fees as business income, a proviso allows capital gains treatment if it is for transferring the right to carry on business.³⁰ The enforceability of non-compete provisions under contract law often centers on the extent of goodwill purchased. The lack of a clear, unified treatment can lead to structures that, in essence, assign values to individual assets like non-compete but are still classified as lump-sum slump sales.³¹

V. Challenges in Distinction and the Need for Clarity

The push-and-pull between commercial objectives like selecting desired assets or structuring consideration for specific benefits and strict statutory definitions of "undertaking" and "going

²⁵ Bharucha & Partners, *Can A Slump Sale Carve-Out Certain Assets And Liabilities?*, Mondaq (Feb. 3, 2023).

²⁶ Ipsita Agarwalla et al., *Business Transfer Why, how and when?*, Nishith Desai Associates.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ The Income Tax Act, 1961 § 28(va).

³¹ Ipsita Agarwalla et al., *Business Transfer Why, how and when?*, Nishith Desai Associates.

concern" creates a grey area. Thus, to aid this ambiguity the regulatory framework is heavily dependent on judicial interpretations, and in turn dependent on judicial discretion which can change on a case-to-case basis.³² This in turn can be inconsistent or subject to appeal, leading to uncertainty. This makes tax planning challenging and can result in litigation.

The ability to exclude non-essential assets or liabilities, in addition with the complexities of allocating lump-sum consideration especially regarding goodwill and non-compete, allows for transactions that resemble asset sales in substance to be formally structured as slump sales to leverage tax benefits like lower capital gains rates or GST exemption. This thus needs to be formulated more clearly to remove or aid this ambiguity to avoid deceptive restructurings.

VI. Conclusion

The current tax and regulatory framework for slump sales in India is a complex and layered process which although has a clear definition and beneficial tax treatment, it still presents several areas of ambiguity that can make it challenging to definitively distinguish between a genuine business transfer and a disguised asset sale. The flexibility allowed in defining "undertaking" and "going concern" through permitted exclusions, the nuances in lump-sum consideration, and the complex interplay with other tax provisions.

For parties involved in M&A, this implies that careful structuring and thorough due diligence are paramount. While slump sales offer significant advantages, particularly tax efficiencies, navigating these complexities requires deep expertise to ensure compliance and mitigate potential risks and liabilities arising from an interpretation that a transaction was merely a disguised asset sale. The ongoing evolution of laws and judicial pronouncements further underscores the need for continuous vigilance and expert advice in this domain.

³² Bharucha & Partners, *Can A Slump Sale Carve-Out Certain Assets And Liabilities?*, Mondaq (Feb. 3, 2023).