UNION BUDGET 2025-26

Benefit of fresh lease life of 8 years to tax losses of amalgamating company: Proposed to be Withdrawn

As per Section 72A and Section 72AA of the Income-tax Act, 1961 (ITA), accumulated loss and unabsorbed depreciation of amalgamating/predecessor company are deemed to be the loss or unabsorbed depreciation arising in the hands of amalgamated / successor company in the year in which amalgamation was affected (emphasis supplied).

Further, Section 72 of the ITA provides that any loss under the head “Profits and gains from business or profession” other than from speculative business can be carried forward for 8 assessment years immediately succeeding the assessment years (AYs) for which the loss was first computed.

The above provision has been interpreted.[1] to the effect that the benefit of carry-forward and set-off of loss of the amalgamating company is available to the amalgamated company for a fresh life of 8 years and unabsorbed depreciation for an unlimited period.

[1]Supreme Industries Ltd. vs. DCIT 2007 17 SOT 476
Hindoostan Mills Ltd. v. Dy. CIT [2023] 294 Taxman 362

Proposed Amendment by Budget 2025:

Budget 2025 proposes to amend section 72A and section 72AA of the Act to provide that any loss forming part of the accumulated loss of the predecessor entity shall be eligible to be carried forward for not more than 8 AY immediately succeeding the AY for which such loss was first computed for the predecessor entity. The explanatory statement to the budget memorandum, states that the proposed amendment is aimed at preventing the evergreening of the losses (i.e., availability of fresh lease life of 8 years in the hands of successor company) and is mainly to bring parity with other companies for whom the benefit is restricted to 8 years.

The amendment is proposed to apply to amalgamations on or after 1 April 2025 (effective date). The effective date is usually understood as the date from which the scheme is given effect by the companies (which date needs to be specifically provided in the scheme). However, there is a confusion regarding the interpretation of 'effective date' as to whether the same should be the date on which the conditions to a scheme are satisfied, when a scheme is approved, or when the scheme is filed.

The amendment is proposed to become effective from 1.4.2026, i.e., AY 2026-27. Accordingly, in all probabilities, the schemes passed on or after 1 April 2025, with the effective date also on or after 1 April 2025, shall be covered by the amendment. A clarity on this aspect would help the taxpayers.

Understanding the Genesis of section 72A:

This provision of section 72A has been on the statute since 1977 and has helped various companies going through distress situations to revive their business and to bring them back to health. The key motivation for introducing section 72A was to save the government from social costs in terms of loss of production and employment and to relieve the government of the uneconomical burden of taking over and running sick industrial units. Initially, the benefit under the section was available only to select units/industries and on approval from specified authorities. With the overall evolution of the economy and industry, in order to encourage rapid consolidation and growth in important sectors, the ambit of the said provision was enlarged over the years, and the conditions for its eligibility, including approvals, were also delegated further.

Even in the current era, we have witnessed acquisitions followed by mergers under CIRP / IBC processes, which have helped bankrupt/distress businesses to revive their health, and the acquirer could use the company's losses to offset its taxable income, leading to some tax savings in the long run.

Thus, as can be seen from above, the benefit under section 72A was a conscious extension of support by the government to encourage the acquirer by extending some tax sops for supporting the government in reviving the sick industry. Thus, this was always considered as a policy-level tax relief extended by the government that too on satisfaction of certain conditions and due approvals. This is also evident from the fact that section 72A, which also covered the transactions of the demerger specifically limited the period of benefit of losses in the hands of the successor company to the remaining period only.

As the law stands today, the benefit is not automatic but is only subject to the satisfaction of conditions that essentially require the continuation and revival of business / capacity utilization by the acquirer. Thus, the proposed amendment does not seem to take into consideration the genesis of the said provision and the socio-economic impact that withdrawal of such provision could create.

Having said the above, various corporates have resorted to acquisition purely to benefit from the tax loss of amalgamating entities or are resorting to internal restructurings such that loss-making entities within the group are merged into profit-making entities to avail the benefit of the above provisions. However, such Merger schemes are heavily challenged by tax authorities before NCLT[2] as well as in the course of normal assessment alleging that the main objective of the scheme is to take benefit of the accumulated losses, and the provisions of the General Anti-avoidance Rule ("GAAR") should be invoked. Thus, the approving authorities are well within their rights to reject a merger scheme where the same is not in the public interest or is not driven by business/commercial objectives.

It is thus expected that the Ministry of Finance should revisit the genesis of the said provisions and reassure the industry of its commitment to support the revival of sick/bankrupt units by relooking at the proposed change.

Nevertheless, where the amendment continues to stay, acquirers will have to reconsider the overall cost-benefit analysis while acquiring sick units/companies. The proposed amendment is likely to impact the M&A industry adversely.

[2] [2022] 138 taxmann.com 570 (NCLT-Chd.) in the case of Panasonic India (P.) Ltd., In re

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