

***IN THE HIGH COURT OF DELHI AT NEW DELHI**

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Date of decision: 21st May, 2013

+ CO.APP. 85/2012, CM No.17764/2012 (for stay) & CM No.17765/2012 (for condonation of delay)

SPENTEX INDUSTRIES LIMITED Appellant

Through: Mr. P.V. Kapur, Sr. Adv. with Mr.
Deepak Diwan, Mr. Aman Anand &
Mr. Sidhant Kapur, Advs.

Versus

INDO RAMA SYNTHETICS (INDIA) LTD Respondent

Through: Mr. Arvind Nigam & Mr. Anoop
Bagai, Sr. Advs. with Mr. Arunabh
Chaudhary, Mr. Raktim Gagoi, Mr.
Surender Kumar Gupta & Mr. Rohit
Jain, Advs.

CORAM :-

HON'BLE THE CHIEF JUSTICE

HON'BLE MR. JUSTICE RAJIV SAHAI ENDLAW

RAJIV SAHAI ENDLAW, J

1. This appeal under Section 483 of the Companies Act, 1956 impugns the judgment dated 23rd July, 2012 of the Company Judge of this Court dismissing Company Application No.762/2009 preferred by the appellant in Company Petition No.4/2003.

2. Company Petition No.4/2003 was preferred by Indo Rama Textiles Limited (IRTL) for sanctioning of a Scheme and which was sanctioned on 27th February, 2003. Simultaneously, the respondent had also approached

the Madhya Pradesh High Court and which also vide order dated 24th March, 2003 sanctioned the Scheme qua the respondent. Under the said Schemes sanctioned by this Court and by the Madhya Pradesh High Court, the spinning business of the respondent was demerged as a going concern and transferred to IRTL, with the respondent retaining the polymer business. IRTL subsequently in or about December, 2006 was amalgamated with the appellant.

3. Company Application No.762/2009 (supra) was filed by the appellant under Section 392(1)(b) for modification of the Scheme qua IRTL sanctioned by this Court on 27th February, 2003 and for a direction to the respondent to transfer certain assets including a part of the housing colony occupied for use by the workers/employees of the erstwhile IRTL to the appellant or in the alternative to pay to the appellant the value of the said assets amounting to Rs.61,30,56,983/-.

4. It was the contention of the appellant before the learned Company Judge that under the Scheme sanctioned by this Court the Undertaking of the spinning business, as a going concern within the meaning of Section 2(19AA) of the Income Tax Act, 1961, was to be transferred to IRTL and for this reason only the respondent had not paid any capital gains tax on the said transfer; that under the said transfer, the properties of the Undertaking being transferred as a going concern, would also stand transferred; that the assets including the housing colony occupied by the workers of IRTL, qua which the application was filed were the assets of the Undertaking of the spinning business; however the Scheme did not mention or refer to the said

assets and thus the Scheme was liable to be modified to make it Section 2(19AA) compliant.

5. The learned Company Judge held, (i) that a reading of the Scheme of Arrangement sanctioned on 27th February, 2003 as a whole showed that the housing colony as well as the common utilities were specifically agreed to be retained and owned by the respondent; (ii) that the properties, buildings and assets that were transferred to IRTL were specifically mentioned; (iii) that the shareholders and creditors of respondent and IRTL had given their consent to the Scheme of Arrangement knowing fully well that the common utilities and housing colony would continue to be retained and owned by the respondent; (iv) that the appellant also at the time of purchasing the shares of IRTL was aware of the Memorandum of Understanding (MoU) signed between the respondent and IRTL subsequent to the sanction of the Schemes and which also specifically stated that the respondent was offering the housing colony to IRTL as a resource for five years upon payment of actual costs; if the respondent was not the owner of the said housing colony and common utilities, there was no question of it offering the same for use to IRTL on payment of costs; (v) that the requirement of Section 2(19AA) would be satisfied if an Undertaking that is being demerged / hived off is a going concern i.e. it constitutes a business activity capable of being run independently in a foreseeable future and for which purpose the Court can examine whether essential and integral assets like plant, machinery and manpower without which it would not be able to run as an independent unit have been transferred to the demerged company or not and Section 2(19AA) does not require all the properties of the Undertaking being transferred to

become the property of the transferee company and non-transfer of some of the previous common assets will not affect the status of IRTL as a going concern; (vi) that before the demerger aforesaid, the respondent company was carrying on both polymer and spinning business and the housing colony and utilities were being used in common for both businesses; that for the Scheme to be Section 2(19AA) compliant did not require transfer of the said common assets also or a share therein; (vii) that it was on the basis of assets/liability transfer basis that the share swap ratio was assessed, determined and allotted and if the housing and common utilities also to be transferred, the share swap ratio may have been different; (viii) that moreover whether or not Section 2(19AA) has been complied with was for the Tax Authorities to determine and if the transfer was not in accordance therewith, it was for the Tax Authorities to levy capital gains if any on the respondent; (ix) that Section 2(19AA) is relevant only for the purpose of determining whether the Scheme is tax neutral and has the consequences for the respondent only; (x) that compliance with Section 2(19AA) cannot be read as a mandatory requirement for all Schemes of amalgamation/arrangement/demerger under Sections 392, 393 and 394 of the Companies Act; (xi) that what the appellant is wanting is re-writing of the Scheme of arrangement which is impermissible under Section 392(1)(b) of the Companies Act; (xii) that when the Scheme was sanctioned in the year 2003, the respondent as well as IRTL were both managed by the same group but the position had since changed; accordingly, Clause 36 of the Scheme providing for arbitration of disputes by the named Arbitrator was

modified to provide for arbitration of the disputes by Arbitrator appointed with the consent of the parties.

6. The senior counsel for the appellant has, (a) taken us through Section 2(19AA) of the Income Tax Act and contended that the test to be complied is whether all the properties of the Undertaking which is to be transferred as a going concern, are being transferred or not and which would include all the properties which the Undertaking has been using till then; (b) contended that the housing colony though situated on leasehold land in the name of the respondent, was being used by the workers of spinning as well as polymer business; (c) contended that the Arbitrator cannot decide how the Scheme is to work and which is the duty of the Court under Section 392(1)(b) of the Companies Act; (d) contended that the MoU signed between the respondent and the IRTL post sanction of the Scheme was not an amendment to the Scheme; (e) contended that there could have been no arbitration clause in the MoU between the respondent and IRTL as no second arbitration clause is permissible and arbitration was already provided for in the Scheme; (f) contended that Clause 6 of the Scheme is inconsistent with Section 2(19AA) of the Income Tax Act; (g) argued that the reasoning of the learned Company Judge in paras 43 and 44 of the judgment is in the teeth of Section 2(19AA); (h) highlighted that even under the Scheme “all other properties” besides those specified in the Schedule, belonging to the undertaking which was being transferred, were transferred; (i) contended that the absence of mention of housing colony and utilities admittedly being used by the Undertaking which was being transferred, necessarily calls for modification of the Scheme and if there is to be any doubt as to whether the housing

colony and the utilities were being used in the business of the Undertaking which was being transferred, an enquiry into that has to be conducted by the Company Court; (j) stated that the MoU was signed between the respondent and the IRTL within three days after sanction of the Scheme with respect to common infrastructure but which did not find mention in the Scheme and which common infrastructure included not only the housing colony but also the club etc.; (k) argued that common utilities cannot include housing colony and the learned Company Judge has wrongly presumed so in para 38 of the judgment as the housing colony is nowhere mentioned in the Scheme; (l) contended that the housing colony was clearly divisible and even if were held to be indivisible, undivided title in the same is deemed to have been transferred to IRTL, on transfer as going concern of the spinning business earlier of respondent, to IRTL; (m) contended that no business activity of spinning can be carried without the workers and which workers necessarily require the housing colony; (n) informed that though the learned Company Judge has held that the Scheme cannot be re-written but has by modifying the arbitration clause re-written the Scheme; (o) argued that the learned Company Judge ought to have amended the arbitration clause in the MoU also, and without the same, the amendment of the arbitration clause in the Scheme does not serve any purpose; reference is made to ***Rustom Cavasjee Cooper Vs. Union of India*** (1970) 3 SCR 530 holding essential staff to be part of Undertaking and it is argued that the same principle would apply to housing colony also; (p) argued that the jurisdiction of the Company Court under Section 392(1)(b) is original jurisdiction; (q) contended that the arbitration commenced by the respondent have either to be stayed or the

award therein to be set aside for the reason of the arbitration clause in the Scheme having been modified; attention is invited to Section 2(47) of the Income Tax Act defining ‘transfer’; (r) contended that the learned Company Judge without making any enquiry whether the housing colony and the utilities are part of business of the Undertaking which was transferred, could not have said whether it was part of the undertaking which was transferred or not; (s) contended that the learned Company Judge in para 46 of the judgment has only partly quoted Kanga, Palkhivala and Vyas’s ‘The Law and Practice of Income Tax’; (t) contended that common utilities can include only electricity and gas and not housing colony.

7. Per contra, the senior counsel for the respondent has, (i) invited attention to the delay of 9 days in preferring this appeal and the reasons given therefor being not sufficient; (ii) stated that both parties had filed written submissions before the learned Company Judge and neither had the appellant argued before the Company Judge on the basis of the Schedule to the Scheme as has been done before us, nor was the same included in the said written submissions; (iii) argued that the jurisdiction of the learned Company Judge while sanctioning a Scheme is different from jurisdiction while dealing with an application under Section 392(1)(b) of the Companies Act; (iv) stated that the Schedule of the Scheme detailing the assets does not mention the housing colony and the site plan filed along with the Scheme also does not include the housing colony; (v) contended that thus the Scheme which has been sanctioned is quite clear that the housing colony was not being transferred; attention is invited to Section 2(42C) of the Act defining slump sale; (vi) argued that a Scheme could be sanctioned only

when the demerged as well as retaining business are going concerns; (vii) argued that non-transfer of shared assets does not negate an Undertaking from being a going concern; (viii) argued that Section 2(19AA) only makes liability to tax neutral and comes into play after demerger; (ix) contended that the transfer is pursuant to the Scheme of Arrangement and Section 2(19AA) does not control the Scheme and the Companies Act does not require the Scheme to be compliant of Section 2(19AA); (x) argued that the objective of Section 2(19AA) is to ensure that there is no sale in disguise of demerger and Section 2(19AA) is concerned with violation of the Income Tax Act and the jurisdiction to determine the said violation is of the Income Tax Officer; (xi) argued that providing accommodation to the staff was not business activity of the spinning undertaking which was hived off; (xii) contended that the expression 'going concern' used in Section 2(19AA) has not been defined but the meaning thereof can be gauged from Section 2(13) of the Income Tax Act defining business and Section 211 (3A) of the Companies Act and the Accounting Standards formulated by the Institute of Chartered Accountants which define the expression 'going concern'; (xiii) stated that foreseeable future has been defined as one year; more than ten years have gone by since the demerger aforesaid and the undertaking of the demerged entity continues to function; (xiv) stated that the balance sheet of the appellant also does not show that the same is not a going concern; (xv) argued that the balance sheet of the first year of the IRTL after amalgamation states that the same has been prepared by following the accounting standards; (xvi) argued that even Section 2(19AA) does not require all the properties of the undertaking to be transferred and only the

property being transferred is required to be property of the transferee; (xvii) contended that the swap ratio of the shares was decided on the basis of the valuation of the assets which were being transferred and in which the housing colony was not included; (xviii) stated that in the Scheme, the assets which were being transferred were mentioned and all the other assets remained with the respondent; (xix) contended that the appellant also at the time of purchasing the shares of IRTL paid the price thereof as per the assets held by IRTL and which did not include the housing colony to which claim is now being made; (xx) has invited attention to the Scheme of Amalgamation of IRTL with the appellant to contend that the appellant thereinunder also did not acquire any right to the housing colony; (xxi) responded that the arbitration clause in the MoU was the same as in the Scheme; attention is invited to the application filed under Section 392(1)(b) to contend that what in fact the appellant is wanting is a money decree; (xxii) argued that though IRTL amalgamated with the appellant in the year 2006, the application under Section 392(1)(b) was filed after three years in May, 2009; (xxiii) contended that even if the Scheme is found to be not compliant with Section 2(19AA), the respondent will suffer the consequence thereof and the same is not a reason for modifying the Scheme; (xxiv) referred to *Premier Automobiles Ltd. Vs. Income-Tax Officer* 264 ITR 193 Bombay on the definition of undertaking; (xxv) relied on *Commissioner of Income Tax Vs. Max India Ltd.* (2009) 178 TAXMAN 196 (P&H) where the Punjab and Haryana High Court concluded that sale of one of its divisions by the assessee was a slump sale since the same was a sale of a going concern even though some of the assets (technical know-how) had

been retained by the assessee-transferer; it is shown that a Special Leave Petition (SLP) thereagainst was dismissed; attention is invited to judgment dated 24th December, 2010 of this Court in ITA No.417/2007 titled ***Commissioner of Income Tax Vs. ECE Industries Ltd***; (xxvi) argued that there can be no order for recovery of money under Section 392.

8. The senior counsel for the appellant in rejoinder has argued, (A) that once the respondent as well as IRTL proclaimed the Scheme to be Section 2(19AA) complaint, they cannot be heard to argue that the only consequence thereof is towards the Income Tax Authorities; (B) that the learned Company Judge has left the arbitration clause in the MoU untouched—if the arbitration clause in the Scheme in view of the changed circumstances was found to be unfair, the learned Company Judge ought to have amended the arbitration clause in the MoU also; it is shown that a prayer in this regard was made.

9. We may notice that the senior counsel for the appellant has also handed over a compilation of judgments but since no specific reference thereto was made during the course of hearing except to ***Meghal Homes (P) Ltd. Vs. Shree Niwas Girni K.K. Samiti*** (2007) 7 SCC 753 and ***S.K. Gupta Vs. K.P. Jain*** (1979) 3 SCC 54, we do not deem it expedient to burden this judgment with the same.

10. We have bestowed our thoughtful consideration to the rival contentions aforesaid. We agree with the reasoning given by the learned Company Judge in the detailed judgment and do not feel the need to reiterate the same and proceed to give only our further analysis of the controversy.

11. Shorn of legalese, the contention of the appellant is that:

- A. though administrative block, SOC Building, Heath Centre, Septic Tank and Sock Pit, Fire Hydrant System, Invertors Chilled Water Plant, Sewage Treatment Plant, Communication System, Computer and Office Equipment and certain other equipment all valued at Rs.8,44,38,916/- and staff and worker colony, DG Set, Electricity sub-Station, Chillers, Part of Administrative block to be completed and Security Barracks valued at Rs. 61,30,56,983/- i.e. total of Rs.69,74,95,899/- were also being used for the spinning business and were essential for the continuance of the spinning business, but were under the Scheme not transferred to IRTL.
- B. that it is not as if IRTL to which spinning business / undertaking earlier of the respondent, was transferred, upon demerger continued to carry on the business without the aforesaid assets; however continued use of the said assets by IRTL for running the spinning business was made possible under the MOU aforesaid;
- C. that since the scheme proclaims to be Section 2(19AA) compliant, the Scheme should, in exercise of powers under Section 392(1)(b), be now be made Section 2(19AA) compliant by transferring rights in the aforesaid assets to the appellant as successor of IRTL or by paying price thereof to the appellant which is the successor of IRTL.

12. However the fact remains that at the contemporaneous time the shareholders of both, respondent and IRTL, did not deem the aforesaid assets as essential to the running of the spinning business/undertaking which was transferred by the respondent to IRTL and felt that the said business could be continued to run by entering into an arrangement for use of the aforesaid assets by IRTL under the MOU aforesaid with the respondent. It is also true that the spinning business, in the last ten years has not stopped to run for the reason of the aforesaid assets having not been transferred by the respondent to the IRTL. From the factum of the appellant itself having agreed to purchase the entire shareholding of IRTL, and which it can safely be presumed must have been after due diligence which would have disclosed that the spinning business being run by IRTL did not have the aforesaid assets of its own but merely had a right to use the same and which right could be taken away at any time, it can safely be presumed that the appellant also did not consider ownership of the aforesaid assets essential to the continued running of the spinning business by IRTL.

13. We are here exercising company jurisdiction dealing with corporate / commercial affairs. Our reasoning/logic cannot be far removed from that of commercial men. When commercial men behind the veil of the appellant felt that the spinning business of IRTL could continue to run even without ownership of aforesaid assets and paid for acquiring the same, we have wondered, whether they can now be heard to urge that the aforesaid assets are so essential to the running of the spinning business so as to make the absence of the same fatal to the running of the said business.

14. Our opinion is clearly no.

15. The filing of the application under Section 392(1)(b) by the appellant after nearly three years of acquiring the said spinning business by purchase of shareholding of IRTL is found by us to be nothing but an act of greed and arm twisting the respondent to continue allowing the appellant to use the said assets. We fail to see, as to how the appellant who had earlier represented to this Court that the assets aforesaid were not essential to the running/operation of the spinning business, can now be heard to the contrary. A change of shareholding of a Company which has in law been conferred the status of a juristic person, does not entitle the company to wriggle out of past commitments/representations. Merely because over the years, the shareholders of the predecessor of the appellant have changed and the predecessor has been amalgamated with the appellant and control and management of the appellant is now with different persons does not entitle the appellant to take a different stand from that taken before this Court earlier.

16. The Supreme Court recently in ***Reliance Natural Resources Ltd. Vs. Reliance Industries Ltd.*** (2010) 7 SCCI has reiterated that the scheme is the commercial wisdom of the parties to the Scheme who have taken an informed decision about the usefulness and propriety of the Scheme by supporting it by the majority vote that has to be kept in view by the Court and the Court cannot act as a Court of appeal and sit in judgment over the informed view of the parties concerned as the same would be in the realm of corporate and commercial wisdom of the parties concerned and the Court

has neither the expertise nor the jurisdiction to dwell into commercial wisdom exercised by creditors and members of the company who have ratified the scheme by requisite majority.

17. We had in this context, during the hearing, inquired from the senior counsel for the appellant whether not it is possible for an industry to arrange for housing for its staff by taking the same on rent and whether not in the present days of lease financing and other complex financial arrangements it is not possibly for an industry to arrange for the equipments etc. by paying rental therefor instead of owning the same. The senior counsel for the appellant agreed. We had next inquired as to in such a case could it be said that the industry would stop running if the said housing facilities or arrangements under which certain plant and equipment was provided were to be withdrawn and whether it would cease to be a running concern. No answer was forthcoming.

18. Not only so, from the appellant having claimed, in alternative to the relief of vesting the aforesaid assets in the appellant by modifying the Scheme, the relief of recovery of monetary value thereof, also it is apparent that the assets qua which application was filed, cannot be said to be essential for the undertaking of the spinning business being a running concern.

19. We are thus of the view that the housing and plant and equipment listed out hereinabove qua which the grievance is made cannot be said to be so essential for the spinning business so as to make the non availability of the same fatal to the running of the spinning business. Such assets, even if needed can also be procured from diverse sources.

20. We may notice that the argument in *Reliance* supra, that gas supply was integral to the Scheme, was held to be unsustainable and it was held that as long as the possibility to run the business remains from alternative sources, it cannot be said that the demerged business has become unviable.

21. Even otherwise, the modifications which the Court can carry out are only to be for the proper working of the Scheme and not for any other purpose and the Court cannot change the basic fabric of the Scheme. A modification for the proper working of the Scheme is distinct from a modification of the Scheme itself and what is permissible under Section 392(1)(b) is the former and not the latter.

22. We are of the view that the modification sought by the appellant is against the fabric of the Scheme and in the domain of modifications of the Scheme and not of modification for working of the Scheme.

23. As far as Section 2(19AA) of the Income Tax Act, on which the entire argument of the appellant hinges, is concerned, we agree with the respondent that for the Court to sanction a Scheme of demerger, compliance of Section 2(19AA) is not essential. The reference to Section 2(19AA) in the Scheme is only for the purpose of making the transaction tax neutral. The same cannot be said to be a pivot around which the Scheme revolved or essential to its workability. We are therefore of the opinion that the non-compliance even if any with Section 2(19AA), would not render the Scheme unworkable.

24. As far as the argument, that because the arbitration clause in the Scheme has been modified, the arbitration clause in the MoU should also be modified is also meritless. The learned Company Judge could not have changed the agreement in the form of MoU between the parties, which was subsequent to the Scheme.

25. We also find that there is no ambiguity in the Scheme and it was not the case of the appellant that the assets aforesaid, under the Scheme stood transferred to the predecessor in interest of appellant and the argument in this regard before us is an afterthought.

26. We in the circumstances aforesaid find the application filed by the appellant before the Company Judge as well as this appeal to be also lacking in *bona fides* and which in our view can be a factor while considering not only the scheme but also at the stage under Section 392(1)(b) of the Act.

27. We accordingly dismiss the appeal with costs of Rs.50,000/- payable by the appellant to the respondent.

RAJIV SAHAI ENDLAW, J

CHIEF JUSTICE

MAY 21, 2013

‘bs/m’..