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

\+ CO.PET. 4/2003

IN THE MATTER OF
M/S. INDO RAMA TEXTILE LTD. ..... Petitioner

Through Mr. P.V. Kapur, Senior Advocate with Mr. Deepak Diwan and Mr. Aman Anand, Mr. V.K. Naoijrath and Mr. Krishna Singhal, Advocates for M/s. Spentex Industries Ltd.

Mr. Arvind K. Nigam and Mr. Anoop Bagai, Senior Advocates with Mr. Arunabh Chaudhary, Mr. Surender Kr. Gupta, Mr. G. Panmei and Mr. Sumit Anand, Advocates for M/s. Indo Rama Textile Ltd.

Reserved on : 31st May, 2012.

% Date of Decision: 23rd July, 2012

CORAM:
HON'BLE MR. JUSTICE MANMOHAN

J U D G M E N T

MANMOHAN, J :

CO. APPL. 762/2009

1. Present application being Co. Appl.762/2009 has been filed under Section 392(1)(b) of the Companies Act, 1956, (hereinafter

referred to as "Act, 1956") on behalf of the Spentex Industries Limited (hereinafter referred to as "Applicant") for modification of a Scheme sanctioned by this Court on 27th February, 2003 as well as for an order directing the respondent-Indo Rama Synthetics Limited (for short "respondent-IRSL") to transfer the assets mentioned in chart in para 13 of the application including the part of the housing colony occupied/used by the workers/employees of Indo Rama Textile Limited (for short "IRTL") to the Applicant or in the alternative to pay to the applicant the value of the aforesaid assets amounting to Rs. 61,30,56,983/-.

2. The relevant facts of the present application are that in 1989 respondent-IRSL was incorporated and it set up a spinning mill in Pithampur, Madhya Pradesh.

3. In 1993-1994, respondent-IRSL set up a second unit in Butibori near Nagpur for expansion of spinning business as well as for commencing polymer production.

4. It is the Applicant’s case that the second unit at Butibori, Nagpur, including the housing colony had been constructed out of the funds of the spinning business.

5. In 2002, respondent-IRSL decided to vertically split its business by way of a Scheme of Arrangement. Under the said Scheme, spinning business was to be demerged as a going concern and transferred to IRTL, while the polymer business was to be retained by respondent-IRSL.

6. On 27th February, 2003, the Scheme qua IRTL was sanctioned by this Court, whereas Madhya Pradesh High Court on 24th March, 2003 sanctioned the Scheme qua respondent-IRSL. The relevant portion of the Scheme is reproduced hereinbelow:-

> *"AND WHEREAS Indo Rama Synthetics (India) Limited ("IRSL") is a public limited company engaged in the manufacture and marketing of Polyester Staple Fibre ("PSF"), Partially Oriented Yarn ("POY"), Fully Drawn Yarn ("FDY"), Textile grade polyester Chip, Draw Texturised Yarn ("DTY") and Spun Yarn. IRSL today is the largest Integrated Polyster Company in India. Its businesses can broadly be classified as Polyster business and Spun Yarn business. IRSL has manufacturing facilities in Pithampur near Indore in Madhya Pradesh and in Butibori near Nagpur in Maharashtra.*
>
> *xxxx xxxx xxxx xxxx*
>
> *AND WHEREAS the Polyester Business having a faster growth potential in India, IRSL has gradually changed its focus from being a Spun yarn manufacturer to becoming an Integrated Polyester producer. As the domestic demand for polyester yarn increased in the 1990s, it expanded its polyester capacity in stages. IRSL also ensured that it keeps improving its operating rates to capitalize on the rising*

domestic demand by judiciously investing in balancing equipment and making process improvements. As a result, the Polyester business of IRSL has witnessed a healthy growth since 1995, when IRSL entered this industry. Currently, IRSL has three production lines for manufacturing PSF, POY & FDY and Polyester Chips.

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AND WHEREAS the two businesses require different management and growth focus. The Polyester business is capital intensive with low manpower requirements. The demand growth is high and IRSL will have to invest in expanding capacity and keeping its capital cost low. On the other hand, yarn business requires more management focus on the mix of products to manufacturers. In terms of the different blends and different counts. Further, the spun yarn division will require a different growth path as compared to the capacity expansion led growth of polyester business. IRSL expects both businesses to achieve substantially higher growth in future through greater focus, induction of suitable technology in existing areas as well as in newer applications and product diversification.

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AND WHEREAS IRSL intends to transfer its business by way of a demerger, to IRTL with the ultimate intent of restructuring and reorganizing the equity capital base under this Scheme of Arrangement with both companies having the same shareholders, in the manner provided herein.

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<u>PART I</u>

1. *Definitions:*

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(iii) 'Appointed Date' means April 1, 2002.

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(vii) "spinning Business" means the entire business of manufacture and sale of cotton yarn, polyester yarn, polyester-cotton and polyester-viscose yarns presently, located at the factory units of the Transferor Company at Pithampur and Butibori and means and includes the following:

(a) All properties and assets, movable and immovable, tangible and intangible, real and personal, corporeal and incorporeal, in possession or in reversion, present and future contingent or of whatsoever nature where-so-ever situated, as on the Appointed Date along with land (as mentioned in Schedule-1) and buildings plant and machinery, capital work in progress, vehicles, equipments, furniture and fittings, sundry debtors, investments inventories, cash and bank balances, bills of exchange, deposits, loans and advances etc. of Spinning Business of the Transferor Company at Pithampur and Butibori as mentioned in Schedule-II.

(b) All leases or parts thereof, tenancy, rights and agency of the Transferor Company, pertaining to the Spinning Business and all other interests or rights in or arising out of or relating to such properties together with all rights, powers, interests, charges, privileges, benefits, entitlements, industrial and other licences (and/or conditions attached thereto), registrations, quotas, trademarks, patents, copyrights, brand names, Import quotas, liberties, easements, advantages pertaining to the Spinning Business, telephones, telexes, facsimile, other communication facilities and equipment, electricity and other such connections, rights and benefits of all agreements and allotments held by or applied for by the Transferor Company after the Appointed Date and pertaining to the Spinning Business and/or to which the Transferor Company is entitled to in respect of the said Spinning Business of whatsoever kind, nature or description held, applied for or may be obtained thereafter or to which the Transferor Company is entitled to in

respect of the Spinning Business together with the benefit of all contracts and engagements and all books, papers, documents and records, related to the said Spinning Business and all rights, obligations, benefits available under any rules, regulations, statutes including direct and indirect taxes and particularly sales tax benefits/exemptions, electricity duty benefits, modvat benefits, import and export benefits and custom duty benefits.

(c) All debts, liabilities, loans and obligations, provisions, deposits present and future, contingent or whatsoever nature, relating to Spinning Business of the Transferor Company as mentioned in Schedule II.

(d) All permanent employees of the Transferor Company engaged in or in relation to and required in the opinion of the Transfer Company's management for the Spinning Business' at the works, factories, branches and other offices etc.

(viii) "The Transferor Company" means Indo Rama Synthetics (India) Limited ("IRSL"), a Company duly incorporated under the Companies Act, 1956 as a public limited company with the Registrar of Companies, Delhi & Haryana on April 28, 1986 having its registered office in New Delhi. The registered office was subsequently shifted to Pithampur, Madhya Pradesh and a fresh Certificate of Incorporation consequent upon change of the registered office of the Company was issued on January 4, 1993. The Transferor Company is having its Registered Office at 51-A, Industrial Area, Sector-III, Pithampur-453001, District Dhar, Madhya Pradesh.

(ix) "The Transferee Company" means Indo Rama Textiles Limited ("IRTL") a Company duly incorporated under the Companies Act,1956 as public limited company with the Registrar of Companies, Delhi & Haryana. The Transferee Company was incorporated under the name Indo Rama Projects and Services Limited on August 2, 1989.

Subsequently, the name was changed to Indo Rama Projects & Investments Limited and a fresh Certificate of Incorporation in the changed name was issued on November 29, 1994. The Company has once again changed its name to its present name and a fresh Certificate of Incorporation consequent upon change of name was issued on July 16, 2002. The Transferee Company is having its Registered Office at Mohan Dev, 13, Tolstoy Marg, New Delhi-110001.

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PART-II

THE SCHEME

Transferred/Demerged Undertaking:

3. With effect from the Appointed Date, all the properties, estates and interests of the Transferor Company in the Spinning Business in its entirety (including but not restricted to its assets, liabilities, rights, licences, benefits, obligations etc.) shall, pursuant to Section 394(2) of the Act and without any further act or deed be transferred to and vested in or be deemed to have been transferred to and vested in the Transferee Company on a "going concern" basis, subject to all existing charges, mortgages, liens, encumbrances, if any created/existing in favour of banks and/or financial institutions and/or other lenders.

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6. The Transferor Company currently generates its own electricity at Butibori for captive consumption for a total of 52,62 MW for the Polyester and Spinning Businesses. Similarly, the Transferor Company provides common utilities to the Spinning Business. Under the Scheme, it is proposed that the Transferor will ensure continuous and uninterrupted supply of electricity and common utilities to the Transferee Company on agreed terms and conditions. Such approvals as may be necessary, shall be obtained from the appropriate authorities by the parties.

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17. The demerger of the Spinning Business as a going concern to the Transferee Company is in accordance with Section 2(19AA) of the Income Tax Act, 1961.

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19. (a) The Transferee Company undertakes to engage on and from the Appointed Date, all permanent employees of the Transferor Company engaged in the Spinning Business on the same terms and conditions at which these employees are engaged as on the appointed Date by the Transferor Company without any interruption of service as a result of the transfer. The Transferee Company also undertakes to accept and abide by any change in terms and conditions that may be agreed/effected by the Transferor Company with all permanent employees between the Appointed Date and Effective Date.

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24. Save and except the Spinning Business of the Transferor Company and as expressly provided in this Scheme of Arrangement nothing contained in this Scheme of Arrangement shall effect the rest of the assets, liabilities and business of the Transferor Company being the Polyester Business which shall continue to belong to and be vested in and be managed by the Transferor Company.

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35. Upon the sanction of the Scheme and after the Scheme has become effective with effect from the Appointed Date the following shall be deemed to have occurred in the sequence and in the order provided:-

(i) The write-off of the accumulated losses against share premium account of the Transferor Company;
(ii) The demerger of the Spinning Business as going concern basis as required under Section 2(19AA) of the Income Tax Act, 1961.

(iii) And conversion of 20% of the Equity Capital of the Transferor Company into Secured Debentures, conversion of 20% Equity Capital into preference shares of the Transferee Company.

36. If any dispute, doubt or difference or issue shall arise between the parties hereto or any of their shareholders, creditors, employees and/or any other person, as to the construction hereof or as to any account, valuation or apportionment to be taken or made of any asset or liability transferred under this Scheme or as to the construction hereof or as to any account, valuation or apportionment to be taken or made of any asset or liability transferred under the Scheme or as to the accounting treatment thereof or as to anything else contained in or relating to or arising out of this Scheme, the same shall be referred to the sole arbitration of Shri O.P. Lohia, resident of R-69, Greater Kailash-I, New Delhi-110048 or any person nominated by him whose decision shall be final and binding. The Courts in New Delhi shall have exclusive jurisdiction in respect of any disputes arising out of or relating to this Scheme.

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SCHEDULE-I

DETAILS OF THE IMMOVABLE PROPERTY OF SPINNING BUSINESS

1. Plot No.51-A

The Plot of land in the Industrial Area No.3,Pithampur, Tehsil Dhar, District Dhar comprising of an area measuring 1,25,000 sq. mts. or there about, held by way of Lease Deed dated July 23, 1988 for a period of 99 years, executed with the Governor of Madhya Pradesh through the Managing Director of Madhya Pradesh Audyogik Kendra Vikas Nigam (MPAKVN), Indore,
The Plot is surrounded by:

On North : Plot No.51-B, Plot No.51-C

On South : 30 mtrs wide Road
On East : 30 mtrs wide Road
On West : 50 mtrs wide Road

2. Plot No.51-B

The Plot of land in the Industrial Area No.3, Pithampur, Tehsil Dhar, District Dhar comprising of an area measuring 40,254 sq. mts. or thereabout, held by way of Lease Deed dated May 25, 1990 for a period of 99 years, executed with the Governor of Madhya Pradesh through the Managing Director of Madhya Pradesh Audyogik Kendra Vikas Nigam (MPAKVN), Indore.
The Plot is surrounded by:
On North : Mhow Neemuch Road
On South : Plot No.51-A
On East : 30 mtrs wide Road
On West : Plot No.51-C

3. Plot No.51-C

The Plot of land in the Industrial Area No.3, Pithampur, Tehsil Dhar, District Dhar comprising of an area measuring 45,000 sq. mts or thereabout, held by way of Lease Deed dated September 1, 1990 for a period of 99 years, executed with the Governor of Madhya Pradesh through the Managing Director of Madhya Pradesh Audyogik Kendra Vikas Nigam (MPAKVN), Indore.
The Plot is surrounded by:
On North : Existing PWD Road
On south : Plot No.51-A
On East : Plot No.51-B
On West : MPEB Plot.

4. Plot No.M-17

The Plot of land in the Industrial Area No.3, Pithampur, Tehsil Dhar, District Dhar comprising of an area measuring 12,500 sq. mts or thereabout, held by way of Lease Deed dated February 17, 1993 for a period of 99 years, executed with the Governor of Madhya Pradesh through the Managing

Director of Madhya Pradesh Audyogik Kendra Vikas Nigam (MPAKVN), Indore.
The Plot is surrounded by:

On North	*:*	*MPAKVN Plot*
On south	*:*	*MPAKVN Plot*
On East	*:*	*80' wide Road*
On West	*:*	*MPAKVN Plot*

5. *Plot No.A-31*

Out of the below mentioned property, an area of 1,10,843.00 sq. mtrs. will remain with Spinning Business as indicated in the attached plan.
All that piece or parcel of land known as Plot No.A-31 in the Butibori Industrial Area within the village limits of Umri & Khape and outside the limits of Nagpur Municipal Corporation, in rural area, Taluka and Registration Sub-District & Registration District Nagpur containing by admeasurement 404607 sq. mtrs or thereabouts. The land is held by way of Lease for 95 years dated July 29, 1994 executed with the Maharashtra Industrial Development Corporation.

The Plot is surrounded by:
On or towards the North by: MIDC Road
On or towards the South by: MIDC Land Plot No.A-31/P
On or towards the East by : MIDC Land Plot No. A-31/P and A-31/2
On or towards the West by: MIDC Boundary and Plot A-31/P-1

SCHEDULE-II

Details of Assets and liabilities of Spinning Business as on April 1, 2002

Total Assets		***(Rs. Lacs)***
1.	*Gross Fixed Assets*	*33,940.87*
	Accumulated Depreciation	*(13,247.04)*
	Net Fixed Assets Including revaluating reserves	*20,693.83*

	Less: Revaluation Reserves	*5,798.46*
	Net Fixed Assets	*14,895.37*
2.	*Capital WIP*	*12.82*
3.	*Deferred Tax Assets*	*1,422.70*
4.	*Inventory*	*2,152.94*
5.	*Debtors*	*1,554.77*
6.	*Cash & Bank*	*47.38*
7.	*Other Current Assets*	*247.45*
8.	*Loans & Advances*	*426.12*
Total Current Assets		*4,428.66*
9.	*Miscellaneous Expenditure*	*96.49*
Total Assets (A)		***20,856.04***
Total Liabilities		
10.	*Current Liabilities & Provisions*	*3,533.19*
11.	*Loan Funds*	*5,938.19*
Total Liabilities (B)		***9,471.38***
Net Worth (A-B)		***11,384.66***"

7. On 28th July, 2005, a Memorandum of Understanding was executed between respondent-IRSL and IRTL for sharing of the common facilities for five years. It only provided for payment of expenses on actual basis by IRTL with no provision for enhancement of fee/rent. In case of dispute, it was agreed that the same would be referred to sole Arbitrator Mr. O.P. Lohia or his nominee. The relevant portion of the Memorandum of Understanding is reproduced hereinbelow:-

"IRSL has agreed to share electricity, common utilities, common infrastructure, common fire fighting facilities & uninterrupted water supply for fire fighting from common storage with IRTL for its Spinning Business located at Butibori as per the Scheme of Arrangement & as per the last MOU dated 31.3.2003 & 18.3.2004.

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Sharing of Expenses between 1.4.2005 to 31.3.2010

1. *The "actual cost" is the basic principle for sharing common expenses between IRSL & IRTL. The Allocation & Ratio of cost sharing between IRSL & IRTL during the period 1.4.2005 to 31.3.2010 under different heads are as per the details mentioned in the enclosed Annexure 'A' & 'B' respectively.*

   1(a) The cost of alteration and interiors including paintings, money plants and minor fixing shall form part of the Annual Maintenance Budget as provided in Annexure A & B.

   1(b) Separate estimates have been agreed to sharing the cost of relocation of PSF and POY in the ratio of 2:3 between IRSL and IRTL respectively as provided in Annexure A & B.

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2. *Validity of contract period*

   This contract is valid for the period 1.4.2005 to 31.3.2010 and will automatically expire on 31.3.2010 and maybe renewed for subsequent period on mutually accepted terms & conditions.

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Allocation Ratio of Cost Sharing between IRSL & IRTL for the period 1.4.2005 to 31.3.2010

Annexure 'A'

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S. No.	*Nature of Services*	*Service Provident Deptt.*	*Basis of Allocation Proposed*
15.	*Housing Colony (Club, Cable TV and Recreation and Security for Colony maintenance etc.)*	*Admin and HR Deptt.*	*Employee Ratio*

8. On 17th February, 2006, present Applicant executed a Share Purchase Agreement with Mr. O.P. Lohia. According to the said agreement, the Applicant and respondent-IRSL were to negotiate mutually acceptable terms for sharing common resources. The relevant portion of the Share Purchase Agreement is reproduced hereinbelow:-

> *"Article 5A*
> *Covenants of the Parties*
>
> *(a) The Parties shall negotiate in good faith, to draw up mutually acceptable terms of sharing, between the Company and IRSL, of the common resources that are currently being shared between them. The terms of sharing shall be such that it ensures that the resources would be available to the Company on such commercial terms as would suffice to be arms length transactions under Indian income tax law and so that the business of the Company is not disrupted."*

9. On 20th December, 2006, a Scheme of Amalgamation of Applicant with IRTL was approved by this Court under Section 391 of the Act, 1956.

10. It is the Applicant's case that in 2007 when respondent-IRSL demanded more money for use of common facilities contrary to the Memorandum of Understanding, the Applicant refused to pay the same. Consequently, the respondent-IRSL withdrew the said facilities.

11. In 2009, respondent-IRSL invoked the arbitration clause in the Memorandum of Understanding dated 28th July, 2005 and appointed its own nomine as the sole Arbitrator.

12. Thereafter, the Applicant applied under Section 14 of the Arbitration and Conciliation Act, 1996 for termination of the arbitrator's mandate. However, on 25th May, 2009, the said application was rejected by a learned Single Judge of this Court. On 20th July, 2009, Applicant's appeal against the said order was also dismissed.

13. On 27th May, 2009, Applicant applied under Section 392(1)(b) of Act, 1956, to this Court seeking a restraint order against respondent-IRSL from disturbing the Applicant's possession or withdrawal of facilities. An ex parte order in favour of the Applicant was passed by this Court.

14. On 10th August, 2009, this Court was pleased to direct that the Arbitrator shall proceed with the matter, but no final award shall be published or pronounced.

15. Mr. P.V. Kapur, learned senior counsel for Applicant submitted that the intention of the Scheme of Arrangement was to transfer to IRTL the undertaking of the spinning business as a going concern within the meaning of Section 2(19AA) of the Income Tax Act, 1961 (hereinafter referred to as "the Act, 1961"). In this connection, he relied upon Clauses 1.1(vii), 3, 17 and 35(ii). He repeatedly emphasised that the respondent-IRSL Company had not paid any capital gains tax on the said transfer.

16. According to Mr. P.V. Kapur, Section 2(19AA)(i) and (vi) of the Act, 1961, stipulated that as a result of the demerger, all the property of the undertaking (as a going concern) being transferred

had to become the property of the resulting company. He, in fact, submitted that in accordance with Section 394(2) of the Act, 1956, the entire undertaking as a whole stood transferred and became the property of the resulting company. He submitted that by operation of law, the title of the properties of the undertaking that vested in the Transferor Company prior to the demerger, upon sanction of the Scheme, stood transferred to the resulting company. He also submitted that the condition precedent of the Act, 1961 was to transfer the property in such a manner that the property transferred became the property of the resulting company.

17. According to him, retaining an undertaking's property and then making it available to the resulting company as a resource under a contract was not in accordance with the statutory requirement.

18. Mr. Kapur stated that if immense costs were to be incurred by the Transferee Company, the transferred undertaking could not be regarded as a going concern apart from the fact that such incomplete transfer would not satisfy the requirement of sub-Section (i) of Section 2(19AA) of the Act, 1961.

19. Mr. Kapur submitted that the law postulated that the undertaking being hived off should be a going concern and it was irrelevant whether the residual undertaking was a going concern or not. According to him, a common asset which could not be divided into two, would have to be transferred to the demerged/hived off undertaking in order to satisfy the requirement of Section 2(19AA) of the Act, 1961.

20. Mr. Kapur pointed out that the Scheme did not refer to the workers/Housing colony or to any infrastructure. Thus, according to him, the workers/Housing colony stood transferred by operation of law to the resulting company (IRTL) as an intrinsic part of the textile undertaking.

21. On the contrary, Mr. Arvind Nigam, learned senior counsel for respondent-IRSL submitted that by virtue of the Amendment of 1999 to the Act, 1961, restructuring of a company involving, inter alia, "demerger" of any Undertaking was treated as tax neutral in terms of Section 2(19AA) of the Act, 1961, subject, inter alia, to fulfillment of the following essential conditions:-

(a) Demerger should have involved transfer of an

Undertaking (as stated in Expl.1) of Section 2(19AA) i.e. (i) transfer of such assets; (ii) such liabilities; (iii) on book values; (iv) the company issued proportionate shares to its shareholders; (v) 3/4th shareholders were shareholders of the resulting company and (b) Transfer of the Undertaking was on a Going Concern basis.

22. According to him, "Undertaking" has been defined in Explanation 1 to Section 2(19AA) of the Act,1961, as any part of the Undertaking, or Unit or Division of the Undertaking; or a business activity taken as a whole; but did not include individual assets or liabilities or any combination thereof not constituting a business activity.

23. Mr. Nigam pointed out that the term "business" has been defined in Section 2(14) of the Act, 1961, to include ".....any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture". He drew attention of this Court to Judicial Dictionary by K.J. Aiyar, 13th Edition defining the term "activity" as under:-

> *"Activity. Read in the context of business, trade or profession, it means the combination of operations*

undertaken by the corporate body, whether or not they amount to a business, trade or profession in the ordinary sense;..."

24. The expression "business activity", thus, according to him meant operations or combination of operations carried on by the Undertaking and constituting a business.

25. Mr. Nigam submitted that the expression "taken as a whole" as explained in the definition of "Undertaking", reproduced supra, was used in the context of "business activity" and not "Undertaking". Therefore, according to him to qualify the pre-requisites of demerger under Section 2(19AA) of the Act, 1961, what was essential was that the unit/division/Undertaking/part of the Undertaking or the business activity as a whole being transferred should constitute a running business, which should be capable of carrying on uninterruptedly with such assets and liabilities alone.

26. Mr. Arvind Nigam further submitted that term "Going Concern" was an accounting concept that implied that the business would continue to exist and operate for an indefinite period in the future. Accounting Standard (AS)-1, issued by the Institute of Chartered Accountants' of India, which dealt with Disclosure of

Accounting Policies, considered "Going Concern" to be one of the generally accepted fundamental accounting assumption underlying the preparation and presentation of financial statements and is:

> *"a. Going Concern The enterprise is normally viewed as a Going Concern, that is, as continuing in operation for the foreseeable future. It is assumed that the enterprise has neither the intention nor the necessity of liquidation or of curtailing materially the scale of the operations."*

27. Statement on Standard Auditing Practices (SAP) 16, "Going Concern", issued by the Council of the Institute of Chartered Accountants of India, provides that -- "When a question arises regarding the appropriateness of the Going Concern assumption, the auditor should gather sufficient appropriate audit evidence to attempt to resolve, to the auditor's satisfaction, the question regarding the entity's ability to continue in operation for the foreseeable future."

28. Mr. Nigam submitted that the fundamental requirement of tax neutral "demerger" was that the Undertaking or any part thereof, being transferred, should be capable of being run independently for a foreseeable future as a Going Concern.

29. It was, therefore, according to him, open to the transferor and the transferee companies to enter into a Scheme of Arrangement

under Sections 391 to 394 of the Act, 1956, wherein the parties may mutually agree to retain any particular asset/liability, even though the same was directly or indirectly, relatable to the Undertaking being demerged.

30. In support of his submissions, Mr. Arvind Nigam relied upon the following decisions:-

A) ***Premier Automobiles Ltd. vs. ITO & Anr. 264 ITR 193 (Bom)*** wherein Bombay High Court held that though certain land was retained, but on analysis, it was clear that the business activity, being a separate line of business of the assessee, was transferred as a Going Concern and therefore, the transaction was that of a slump sale. The Bombay High Court observed that *" ....under the said law, the basic test which one must apply to ascertain whether there existed a slump sale is continuity of business. The question to be asked is whether there is a transfer of business as a whole?.....The question therefore to be asked is: whether there was a transfer of land, building, plant and machinery as a whole or whether there was a transfer of land, building or plant and machinery separately*

and individually. For that purpose, one has to read the terms and conditions of the arrangement.....one has to construe the entire arrangement in order to ascertain the true intention of the parties and merely because there is a schedule of assets on record, it cannot be said that there is a sale of itemized assets."

B) ***CIT v. Max India Ltd. 319 ITR 68 (P&H),*** wherein the Punjab and Haryana High Court held as under:-

> *"3. We have heard learned counsel for the parties and perused the record.*
>
> *4. In para 20 of its order, the Tribunal held that the sale was slump sale if it was a sale of Going Concern, even if some of the assets were retained by the transferor..... Para -29 of the order is reproduced below:*
> *29. From the above, it is evident that for a sale to be termed as a 'slump sale', it is not essential that all the assets and liabilities must be transferred. Even if some assets and liabilities are retained by the transferor, the sale would not lose the character of being a slump sale, if the transfer is of a Going Concern, on that basis and the transferee is in a position to carry on the business without any interruption. In the present case, the right to use the technical know-how developed by the assessee was granted by the assessee to the transferee against the payment of a separate consideration. The proprietary rights therein were retained till 30-6-2000. On facts, in view of the above numerous judicial pronouncements, it cannot be said that what the transferee acquired was not a Going Concern. Rather, after the transfer, the*

transferee carried on the business without any disruption therein. In West Coast Chemicals & Industries Ltd.'s case (In Liquidation), F.X. Periera & Sons (Travancore) (P) Ltd.'s case, Premier Automobiles Ltd.'s case and Raka Food Products' case, amongst others, it has been held that in the case of a sale of an Undertaking as a whole, on a Going Concern basis, if some assets are retained by the transferor or some liabilities are not taken over by the transferee, this fact does not render the slump sale as not a slump sale.

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13. The view of the Tribunal is, thus, consistent with the settled law."

C) ***CIT vs. ECE Industries Limited in ITA No. 417 of 2007,*** this Court affirmed the following reason given by the Tribunal while holding that the transaction in question was a slump sale.

"35.....

(viii) The approach adopted by the ld. CIT(A) for rejecting the version of the assessee regarding the slump sale on the reasoning that for slump sale there should be sale of entire or whole business of the assessee including all the undertakings even though they may be self sufficient and independent units, is not correct because the word 'slump sale' as interpreted by various authorities and as defined in Section 2(42C) means 'transfer of one or more undertakings' as a result of the sale for a lump sum consideration without values being assigned to any assets and liabilities. Although this definition has been brought in Section 2(42C) by the

amendment introduced with effect from 1-4-2000 but the concept behind slump sale has been the same even before the amendments has been held by various courts."

D) ***Rohan Software (P) Ltd. v. ITO, 115 ITD 203 (Mum.),*** wherein the Tribunal held *"the sale of software business including intellectual properties, etc; but excluding building and motor car did not militate the concept of slump sale."*

31. Consequently, Mr. Arvind Nigam submitted that there was no requirement in law that each and every asset and liability directly or indirectly relatable to the demerged Undertaking should be transferred in the Scheme of Demerger. Accordingly, he submitted that if the Undertaking or any part thereof, being transferred independently constituted a running business, which was capable of carrying on as a Going Concern, the same would be regarded as tax compliant demerger.

32. Mr. Arvind Nigam lastly contended that under the Scheme of Demerger agreed upon between the parties, certain flats in the housing colony occupied by the employees of the demerged Undertaking were not transferred as transfer of the said flats was not

crucial/critical affecting the ability of the demerged undertaking to continue its business as a Going Concern. Mr. Nigam pointed out that even at the time of demerger, only around 20% of the employees of demerged Spinning business were actually residing in those flats and rest were staying in either rented or own accommodation outside the housing colony. According to him, the Applicant had carried on business of the demerged Undertaking uninterruptedly for nearly a decade without transfer of the housing colony and consequently, he stated that the present application was devoid of merits.

33. In rejoinder, Mr. P.V. Kapur, learned senior counsel for Applicant submitted that for the purposes of ascertaining the true intent of the parties, Section 2(19AA) of the Act, 1961 had a bearing. According to him, it was represented to the shareholders of the company as also to this Court in 2003 that all the assets of the undertaking within the meaning of Section 2(19AA) of the Act, 1961 were being transferred in such a manner that their title would stand transferred to and vested in IRTL and it was on this representation and understanding that the then Company Court sanctioned the Scheme of Arrangement.

34. Mr. P.V. Kapur further submitted that the judgments relied upon by Mr. Arvind Nigam, learned senior counsel for respondent-IRSL were inapplicable to the facts of the present case as they dealt with issues relating to ‘slump sale’ and not ‘demerger’. He pointed out that the ingredients of 'slump sale' and 'demerger' were different. He also contended that most of the judgments cited by Mr. Nigam belonged to a period when neither 'demerger' nor 'slump sale' definitions existed in the statute.

35. Having heard the parties at length, this Court is of the view that the Scheme of Arrangement sanctioned by this Court in 2003 has to be read as a whole and not in a piecemeal manner. The Applicant is reading the Scheme of Arrangement as if it comprises only one clause, namely, Clause 17.

36. With respect to the Applicant, the Scheme of Arrangement does not revolve around Section 2(19AA) of the Act, 1961 and the rest of its Clauses are not otiose.

37. In fact, upon reading the Scheme of Arrangement in its entirety, in particular Clauses 1.1(vii), 3, 6, 24 along with the Schedules and map annexed to it, this Court has no hesitation in

concluding that the Housing colony as well as common utilities were specifically agreed to be retained and owned by respondent-IRSL. The properties, buildings and assets that were transferred to IRTL under the Scheme of Arrangement were specifically mentioned in its Schedule 1 and 2.

38. This Court is of the view that shareholders and creditors of respondent-IRSL and IRTL gave their consents to the Scheme of Arrangement knowing fully well that common utilities and housing colony would continue to be retained and owned by the respondent-IRSL.

39. Even the Applicant before entering into the share purchase agreement was aware of the Memorandum of Understanding dated 28th July, 2005, which specifically stated that housing colony was being offered by respondent-IRSL as a resource to IRTL for five years upon payment of actual cost. In the opinion of this Court, if respondent-IRSL was not the owner of the common resources and infrastructure, there was no question of it offering the common assets for use to IRTL on payment of cost.

40. Since considerable emphasis was laid by the Applicant's senior counsel on Section 2(19AA) of the Act, 1961, the same is reproduced hereinbelow for ready reference:-

> *"2.Definitions.-In this Act, unless the context otherwise requires, -*
>
> *xxx xxx xxx xxx*
>
> *(19AA) "demerger", in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956 (1 of 1956), by a demerged company of its one or more undertakings to any resulting company in such a manner that--*
>
> *(i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;*
>
> *(ii) all the liabilities relatable to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;*
>
> *(iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;*
>
> *(iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis;*
>
> *(v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or,*

its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;

(vi) the transfer of the undertaking is on a going concern basis;

(vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section 72A by the Central Government in this behalf. "

Explanation 1.--For the purposes of this clause, "undertaking" shall include any part of an undertaking, or a unit or 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."

41. Upon reading of the aforesaid Section, it is apparent that the definition of Demerger in Act, 1961, would be satisfied if the undertaking that is being demerged is hived off as a going concern, that means, if it constitutes a business activity capable of being run independently for a foreseeable future. To ensure that it is a going concern, the Court while sanctioning a Scheme can certainly 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.

42. However, this Court is not in agreement with the Applicant's submissions that in a Scheme of Demerger by virtue of Section 2(19AA) of the Act, 1961, all the properties of the undertaking become the property of the resulting company. This Court is of the view that non-transfer of some of the pervious common assets being used by the transferee undertaking will not affect IRTL status as a going concern.

43. In fact, it is settled legal position that there is no requirement under the provisions of the Act, 1961 or Act, 1956 for transfer of all common assets and/or liabilities relatable to the Undertaking being demerged. The Applicant's submission that all common assets that cannot be divided must be transferred to the transferee namely, IRTL overlooks the explicit language of Section 2(19AA)(i) of the Act, 1961, which states that "*all the properties of the undertaking being transferred by the demerged company, immediately before the demerger becomes the property of resulting company by virtue of the demerger"*. The expression "*being transferred*" is relatable to such assets as are being transferred to make it a going concern. Moreover, if the applicant's submission is accepted it would put all

the schemes of demerger in a 'straightjacket' format and it would also infringe upon the two company's freedom to negotiate with regard to the transfer of common assets. This Court is of the view that while framing a scheme of demerger, the existing and the resulting companies after ensuring that both of them are a going concern, are free to negotiate which common asset/liability would be transferred to which undertaking. After all, it is on this asset/liability transfer basis that share swap ratio are assessed, determined and allotted.

44. The Applicant's submission also overlooks the primary function of the Company Court, namely, to ensure that the Scheme serves larger public interest, that means, to ensure both the existing and resulting unit are economically and technically viable. Consequently, merely because certain common assets and liabilities have not been transferred, the transaction would not cease to be demerger of an Undertaking, provided the assets and liabilities transferred, by themselves, constitutes a running business and the business can be carried on uninterruptedly with such assets and liabilities alone.

45. Moreover, the Applicant's contention that Clause 6 of the Arrangement must be struck down as it is contrary to Clauses 17 and 35, is beyond the pleadings of the case. It is also pertinent to mention that no direction has been sought by the Applicant for continued sharing of common resources and common infrastructure.

46. In 'The Law and Practice of Income Tax' by Kanga, Palkhivala and Vyas, it has been observed that "the provisions relating to taxation of the companies involved in the demerger and their shareholders are applicable only if the demerge fulfils the Section 2(19AA) of the Act, 1961. Mere sanction of the High Court for demerger under the Act, 1956, is, by itself, not sufficient".

47. Therefore, whether or not Section 2(19AA) of the Act, 1961 has been complied with, is not to be determined pre-merger, but post merger and that too by the tax authorities. In the opinion of this Court, if the Scheme of Arrangement is not tax complaint, then the tax authorities will levy capital gains tax, if any, on the transferor, namely, respondent-IRSL**.**

48. Accordingly, compliance with Section 2(19AA) of the Act, 1961, is relevant only for the purposes for determining whether the

Scheme is tax neutral or not and it has consequences for respondent-IRSL only.

49. Consequently, the contention urged by the Applicant that in view of Section 2(19AA) of the Act, 1961, the Scheme of Demerger must necessarily comply with Section 2(19AA) which is meant for availing tax concession cannot be read as a mandatory requirement for all schemes of amalgamation/arrangement/de-merger under Sections 391/392/394 of the Act, 1956. The said provision cannot be read and interpreted to include assets/units/undertakings/business belonging to the respondent-IRSL which were never transferred or intended to be transferred to IRTL and which are not mentioned in the Scheme of Arrangement. In the opinion of this Court, the Applicant is in error in contending that the common infrastructure is liable to be made over to them by virtue of reasoning of Section 2(19AA) of the Act, 1961 as the division of assets was indicated in the Scheme.

50. This Court is also of the view if the Applicant's interpretation of Clause 17 of this Scheme of Arrangement which refers to Section 2(19AA) of the Act, 1961 is accepted then it would amount to re-

writing the Scheme of Arrangement, which this Court cannot do in the present proceedings. In fact, the Supreme Court in ***S.K. Gupta and Another vs. K.P. Jain and Another (1979) 3 SCC 54*** has held as under:-

> *"13. When a scheme is being considered by the Court, in all its ramifications, for according its sanction, it would not be possible to comprehend all situations, eventualities and exigencies that may arise while implementing the scheme. When a detailed compromise and/or arrangement is worked out, hitches and impediments may arise and if there was no provision like the one in Section 392, the only obvious alternative would be to follow the cumbersome procedure as provided in Section 391(1), viz., again by approaching the class of creditors or members to whom the compromise and/or arrangement was offered to accord their sanction to the steps to be taken for removing such hitches and impediments. This would be unduly cumbersome and time-consuming and, therefore, the legislature in its wisdom conferred power of widest amplitude on the High Court under Section 392 not only to give directions but to make such modification in the compromise and/or arrangement as the Court may consider necessary, the only limit on the power of the Court being that such directions can be given and modifications can be made for the proper working of the compromise and/or arrangement. The purpose underlying Section 392 is to provide for effective working of the compromise and/or arrangement once sanctioned and over which the Court must exercise continuous supervision [see Section 392(1)], and if over a period there may arise obstacles, difficulties or impediments, to remove them, again, not for any other purpose but for the proper working of the compromise and/or arrangement.*

This power either to give directions to overcome the difficulties or if the provisions of the scheme themselves create an impediment, to modify the provision to the extent necessary, can only be exercise so as to provide for smooth working of the compromise and/or arrangement. To effectuate this purpose the power of widest amplitude has been conferred on the High Court and this is a basic departure from the scheme of the U.K. Act in which provision analogous to Section 392 is absent. The sponsors of the scheme under Section 206 of the U.K. Act have tried to get over the difficulty by taking power in the scheme of compromise or arrangement to make alterations and modifications as proposed by the Court. But the legislature, foreseeing that a complex or complicated scheme of compromise or arrangement spread over a long period may face unforeseen and unanticipated obstacles, has conferred power of widest amplitude on the Court to give directions and, if necessary, to modify the scheme for the proper working of the compromise or arrangement. The only limitation on the power of the Court, as already mentioned, is that all such directions that the Court may consider appropriate to give or make such modifications in the scheme, must be for the proper working of the compromise and/or arrangement."

(emphasis supplied)

51. From the aforesaid, it is apparent that in the proceedings under Section 392(1)(b) of the Act, 1956, the Court cannot rewrite the scheme approved in the meeting called under Section 391(2) of the Act, 1956; but, it can only make such modification as it may consider necessary for proper working of the compromise or

arrangement.

52. It is pertinent to mention that when the scheme was sanctioned in the year 2003, both the Transferor and Transferee Companies were owned and managed by O.P. Lohia group but now both the entities are owned and managed by different business groups. Consequently, to ensure that the scheme sanctioned by this Court is properly implemented, this Court modifies only the dispute redressal mechanism in Clause 36 of the Scheme by directing that in the event of any dispute, doubt or issue arising between the parties, the same shall be referred to a sole arbitrator to be appointed with the consent of the parties. If, however, no consensus is reached between the parties, then the sole arbitrator shall be appointed by the concerned Court. Accordingly, Clause 36 of the Scheme shall now read as under:-

> *"36. If any dispute, doubt or difference or issue shall arise between the parties hereto or any of their shareholders, creditors, employees and/or any other person, as to the construction hereof or as to any account, valuation or apportionment to be taken or made of any asset or liability transferred under this Scheme or as to the construction hereof or as to any account, valuation or apportionment to be taken or made of any asset or liability transferred under the Scheme or as to the accounting treatment thereof or as to anything else contained in or relating to or arising out of this Scheme, the same shall be referred to the sole arbitrator to be*

nominated jointly by both the parties. The Arbitrator's decision shall be final and binding. If, however, there is no consensus upon the name of the sole arbitrator, the sole arbitrator shall be appointed by the concerned court. The Courts in New Delhi shall have exclusive jurisdiction in respect of any disputes arising out of or relating to this Scheme."

53. With the aforesaid modification, the present application stands disposed of.

MANMOHAN,

JULY 23, 2012
js/rn