BOMBAY HIGH COURT

Commissioner of Income-Tax

Vs.

Gaekwar Foam and Rubber Co., Ltd

I.T. Ref. No. 13 of 1958

(S.T. Desai and K.T. Desai, JJ.)

03.10.1958

JUDGMENT

S.T. Desai, J.

1. A short but interesting question of construction of Section 15C of the Income-tax Act arises for our determination on this reference, which comes before us at the instance of the Commissioner of Income-tax, Bombay, under Section 66(1). The facts may be briefly stated. A partnership firm consisting of three partners started doing business of manufacturing shoes from 1-7-1948 in the firm name of "Coral and Co." There was another concern - The Gaekwar Foam and Rubber Co. which was a limited liability company registered on 21-7-1949. Owing to devaluation of currency, this latter company had difficulties in carrying on its business of foam rubber. It came to the notice of this company, which is the assessee company before us, that the firm of Goral and Co. wanted to sell its business. The assessee company took over all the assets of the business of Coral and Co. including its goodwill for the consideration of Rs. 1,50,000/-. The payment was not made in cash but was by allotting 1500 shares of the face value of Rs. 100/- each to the three partners in the firm of Coral and Co. The nominal capital of the assessee company was Rs. 5,03,000/- divided into 5000 ordinary shares of Rs. 100/- each and 3000 'B' shares of Re. 1/- each. Neither the credits and out standings nor the debts and liabilities of Coral and Co. were taken over by the assessee company. We shall refer to the agreement, which is one of sale, little later in our judgment. In respect of the assessment year 1952-53, the assessee company claimed the benefit of an exemption from tax under Section 15C on the ground that it was a newly established industrial undertaking. The Income-tax Officer rejected the assessees contention. According to him, the assessee company was formed by reconstruction of a business already in existence and, therefore, the assessee company was not entitled to the benefit of Section 15C claimed by it. The Appellate Assistant Commissioner took the contrary view. His conclusion was that this was a case of transfer of building and machinery to a new business and as the business of the transferor came into existence after 1-4-1948, the assessee was entitled to

the exemption claimed by it. The matter was carried in appeal by the Department and the Tribunal took the view that the Appellate Assistant Commissioner was right in the conclusion reached by him. In its order, it stated :

> "If we were to accent the contention of the Department, it will only mean that the whole object of the provision made has been frustrated. With a view to help the building up of new industries, it has been provided that industries started after 1-4-1948 will get some special benefits. The Income-tax Officer would have been right in not allowing the exemption if the business taken over by the assessee had been commenced prior to 1-4-1948. The exemption is attached to the business and not to the assessee. It matters little if the business changes hands six times over a period of one year. As long as the industrial undertaking commenced business after 1-4-1948, it will, in our opinion, be entitled to claim the benefit of Section 15C."

The question we are called upon to answer on this reference is :

> "Whether on the facts and in the circumstances of the case, the assessee company is entitled to relief from tax under Section 15C of the Income-tax Act ?"

2. It has been argued before us by Mr. G.N. Joshi, learned Counsel for the Revenue, that the Tribunal was in error in interpreting clause (i) of Sub-Section (2) of Section 15C. The argument' briefly stated was that this was a case of an industrial under-hiking formed by reconstruction of a business already in existence and if it was a newly established industrial undertaking, which was formed by reconstruction of a business already in existence, it could not claim the exemption granted by Section 15C. It will be convenient at this stage to set out that part of Section 15C which is material for the purpose of this Reference :

> "(2) This section applies to any industrial undertaking which -
> (i) is not formed by the splitting up, or the reconstruction of, business already in existence or by the transfer to a new business of building, machinery or plant used in a business which was being carried on before the 1st day of April, 1948."

In Sub-Section (2) there are two other clauses and there is a proviso to this Sub-Section. But it is not necessary to set out the same because they have little bearing on the part of Section 15C which we are called upon to interpret in this reference. Clauses (ii) and (iii) relate to certain periods and to the number of workmen employed by the industrial undertaking and the proviso empowers the Central Government by a notification to direct that the exemption cannot be availed of by any particular industrial undertaking.

3. The argument of Mr. Joshi is that an assessee who wants to avail of the benefit of the exemption must fulfill all the conditions and requirements of the Section. That proposition is not

disputed. Then, the argument has proceeded that in clause (i) there are three requirements or conditions. We agree with Mr. Joshi that all the three requirements or conditions specified in clause (i) of Sub-Section (2) must be satisfied before an assessee can claim the benefit of the exemption granted by the Section and the argument in effect has been that since this is a case of reconstruction of a business already in existence, the assessee cannot get any relief. It is suggested by Mr. Joshi that the words at the end of clause (i) : "before the 1st day of April, 1948" apply to the third condition or requirement of clause (i) of Sub-Section (2) and not to all the three conditions or requirements specified in that clause. On the other hand, it has been suggested by Mr. Palkhiwalla that those words apply to all the three requirements or conditions of that clause. It is not necessary for us to decide on this reference whether the words "before 1-4-1948" apply to all the three conditions or requirements of clause (i) of Sub-Section (2). We shall, therefore, confine our consideration only to the point, which is directly before us, namely, whether this is a case of reconstruction of a newly established industrial undertaking formed by reconstruction of a business already in existence. If it is not a newly established industrial undertaking formed by reconstruction of a business already in existence, the assessee must succeed because it is not the contention of Mr. Joshi that this is a case of an undertaking formed by splitting up of a business already in existence nor is it the contention of Mr. Joshi that this is not a case of an undertaking formed by transfer to a new business of building, machinery or plant used in a business which was being carried on before 1-4-1948. Mr. Joshi has taken us through the various clauses of the agreement between the firm of Coral and Co., the vendors and the assessees. On the face of it, it is an agreement of sale of the assets of building, machinery and plant of an industrial undertaking and also of the stock-in-trade of that firm, as we shall presently point out. The sale includes the goodwill of the vendor firm. What is kept out however is the credits and out standings of the vendor firm and its debts and liabilities. Clause (2) refers to the nominal capital of the transferee company, the assessee. Clause 3(1) speaks of the operation of the sale and purchase as from 1-3-1950. The agreement is dated 28-2-1950. Then, the goodwill of what is described as "the late company" is mentioned. Then, the right to use the premises occupied by the vendors is mentioned. Next is mentioned the plant, machinery, furniture and other tools of the vendors. Consideration is mentioned thereafter as being Rs. 1,50,000/- to be paid and satisfied by the allotment to the vendors of 1500 fully paid up ordinary shares of the assessee company of the face value of Rs. 100/- each. The price of the plant, machinery etc. is shown as agreed upon at Rs. 1,43,758 and the goodwill at Rs. 6,242/-. Then there is a reference to the credits and out standings and the debts and liabilities of the vendor firm, to which we have already made reference. Then there is stipulation about the indemnity given to the purchaser by the vendors against any proceedings, claims and demands in respect of their debts, liabilities, contracts and previous engagements and in respect of tax. As to stock-in-trade, it is mentioned that it was a matter left to the transferee company whether it should take it up or not. Lastly there is a. restrictive condition which restrains the vendors from carrying on a competing business within the area of 100 mile, of Bombay. On these stipulations and conditions in the agreement of sale, it is argued by Counsel for the Revenue that this is clearly a case of reconstruction of a business already in existence. Considerable emphasis has been laid by Mr. Joshi on the expression

"business" and we propose to bear in mind the importance we are asked to attach to the business of the vendors. It is said that here the goodwill has been transferred. It is said that although the out standings and liabilities were not taken up, that made no difference. It is then said that the fact that the stock-in-trade was not taken up at the time of the sale made little difference. The argument has been that what is of importance and consequence is that all the assets of the vendor firm were taken up as going concern. Now, we do not think we would be justified in reading this agreement as one under which all the assets of the vendor firm were taken up by the assessee company as a going concern. But at the same time it is true that the premises where its business was being carried on and all the plants, machinery, furniture and other tools of the vendor firm were taken up by this agreement described as one of sale. Then it is said that it was the same persons who are carrying on the business of the assessee company. Here we are unable to accept Mr. Joshi's suggestion. We have carefully read the agreement and the Statement of the case and there is nothing to suggest that it is the same persons, that is, the vendors who are carrying on the business of the assessee company. No such fact has been found by the Tribunal. The capital of the assessee company, as we have already mentioned is Rs. 5,03,000/- and the consideration was that the vendors were to get only 1500 ordinary shares of the face value of Rs. 100/- each allotted to them in payment of consideration. Then it is said that the identity of the vendor firm was completely merged in the assessee company. It cannot be said that this was a case of amalgamation or identity of the vendor firm being merged in the assessee company if it was a transaction of sale. What appears to have happened is that the vendor firm sold its plant, machinery, furniture and tools and ceased to carry on its business. It is the case of a business of a firm ceasing after the sale of its machinery, plant, etc. when it could not possibly carry on business. The goodwill of that firm, as we have already said, was sold to the assessee company.

4. The argument of Counsel for the Revenue is that in view of the stipulations and conditions mentioned in the agreement, this is a case simply of reconstruction of the business of the vendors firm. Learned Counsel stated that a business is reconstituted when it is carried on after the liabilities of the business which made it difficult to carry on are removed, that is, when the burden of debts is removed and it starts with a clean state. Then it is said that the dictionary meaning of the expression "reconstruction" is "to rebuild or to reconstitute" and says Mr. Joshi, this is a business "which is reconstituted or rebuilt".

5. The question before us, therefore, is : Is this a case of reconstruction of a business already in existence? Now, it is clear that all the conditions and requirements of sub-clause (i) of Sub-Section (2) must be satisfied before the benefit of the exemption can be claimed by a newly established industrial undertaking. The section does not apply and the exemption cannot be claimed by an assessee if the industrial' undertaking is formed by splitting up of its business or by reconstruction of its business or in case of transfer to a new business of building, machinery or plant used in a business which was being carried on before 1-4-1948.

6. The expression "reconstruction" represents a legal conception. It has been used in statutes

relating to company law but even there, as we shall point out, little later in our judgment, no judge has ever attempted to give a comprehensive definition of that expression. The Income-tax Act does not define the expression. This is just as well since it seems difficult to have a definition which may aptly meet with every particular instance and it seems permissible to enter a caveat against any judicial attempt at a definition exclusive or inclusive of a legal expression which as has so often been said, has not precise meaning. The expression though difficult to define, may be described without difficulty.

7. It is well established that the words which express a legal conception must have attributed to them their legal meaning. Technical words, where we find them, must have their technical sense ascribed to them and not their popular sense-uti loquitor vulgus. The principle is of cogency when the words in question represent legal conceptions. The reconstruction of a business or an industrial undertaking must necessarily involve the concept that the original business or undertaking is not to cease functioning and its identity is not to be lost or abandoned. The concept essentially rests on changes but the changes must be constructive and not destructive. There must be something positive about the whole matter as opposed to negative. The underlying idea of a reconstruction evidently must be and this is brought out by the section itself of a "business already in existence." There must be a continuation of the activities and business of the same industrial undertaking. The undertaking must continue to carry on the same business though in some altered or varied form. If the alterations and changes are substantial there would be little scope for describing what emerges sis a reconstruction of the business. Thus for instance if the ownership of a. business or an undertaking changes hands not ostensibly but in reality and effectively, that would not be reconstruction or if the very nature of the business is changed, that again would not be reconstruction. On the other hand, reorganization of the business on sounder lines or alterations in the mode or method or scope of the activities of the business or in its personnel or infusion of new blood in the management or control of the business which may even be fry some changes in the constitution of persons interested in the undertaking would certainly be no more than reconstruction of the business if it is substantially the same business carried on by substantially the same persons.

8. Now, support is to be derived for the view we take of the interpretation of the material words of clause (i) of Sub-Section (2) of Section 15C from certain observations of Mr. Justice Buckley, as he then was, in He South African Supply and Cold Storage Company, (1904) 2 Ch 268. We may immediately observe that the word "reconstruction" was being considered by the Court in that case in the context of Company law and in referring to these observations we are conscious of the fact that the observations are not made in the self same context but even so they are general observations which can be of guidance and assistance if taken as no more than stating a broad general principle and coming from an authority like Lord Wrenbury we think they are entitled to be read with respect. At p. 286 of the Report in that case the learned Judge was considering the question of reconstruction "of an undertaking". He observes :

> "What does "reconstruction" mean ? To my mind it means this. An undertaking of some definite kind is being carried on and the conclusion is arrived at that it is not desirable to kill that undertaking, but that it is desirable to preserve it in some form and to do so, not by selling it to an outsider who shall carry it on that would be a mere sale but in some altered farm to continue the undertaking in such manner as that the persons now carrying it on will substantially continue to carry it on. It involves, I think, that substantially the same business shall be carried on and substantially the same persons shall carry it on. But it does not involve that all the assets shall pass to the new company or resuscitated company, or that all the shareholders of the old company shall be shareholders in the new company or resuscitated company. Substantially the business and the persons interested must be the same. Does it make any difference that the new company or resuscitated company does or does not take over the liabilities ? I think not. I think it is none the less if reconstruction because from the assets taken over some part is excepted provided that substantially the business is taken and it is immaterial whether the liabilities are taken over by the new or resuscitated company or are provided for by excepting ......'

Later on, the learned Judge observes that

> "it is not vital that either, the whole assets should be taken over or that the liabilities should be taken over."

We have to see whether substantially the same persons carry on the same business; and if they do, that, I conceive, is a "reconstruction". Now fully appreciating the distinction which Counsel for the Revenue has sought to make between the case of a reconstruction of a company and the case of reconstruction of a business, these observations as we read them, are equally illuminating in the context of reconstruction of a business already in existence in the case of a newly established industrial undertaking. In fact the learned Judge speaks of an undertaking of some definite kind being carried on. The emphasis, it will be noticed, is on two things when substantially the same business was carried on and substantially the same persons were carrying it on. It is also to be noticed that the learned Judge draws a clear distinction between the reconstruction and a sale of an undertaking. In the case of a sale, there can be no question of reconstruction. Now, in these matters, we have to look at the substance of the transaction and not the form. If looking at the substance of the transaction, it is a sale, then the concept of reconstruction must be ruled out for in such a case there is no scope for speaking about any reconstruction of an existing business. It is not necessary to pursue the question of reconstruction in the context of the Company law because in this case we are not concerned with any such question and it is not necessary, therefore, to refer to the observations on the point of the leading text book writers on the subject of Company law in England.

9. Now, there are some other words in this clause to which also we are bound to attach some importance. The clause speaks of a newly established industrial undertaking formed by the

reconstruction of its business already in existence. In the forming of this industrial undertaking those, who owned the original business, must have a large say if they reconstruct it. Speaking broadly it is they who can be said to reconstruct the company in any such case and if it is floating of a new company it is they who can be said to have floated a new company for their business which was already in existence. It would be a misnomer to speak of a buyer of an undertaking reconstructing the vendor's business. He may reconstruct his own business thereafter. But that would be a totally different matter. Can it, therefore, be said on the facts of his case that it was the vendors who have formed a new company by reconstruction of a business which was ready in existence ? Here is a case of transfer of building, machinery, plant and other implements of a shoe factory. The agreement is both in substance and in form one of out and out sale. The only relation that remained between the vendors and the lessee Company which thereafter carried on its business in the name of Carona Shoe and Co. is that the vendors became some of the shareholders in the assessee company they having been allotted 1500 ordinary shares of the face value of Rs. 100/- each. There is little scope for doubt or difficulty in interpreting the relevant part of clause (i) of Sub-Section (2) and it is not necessary for us, therefore, to discuss in any detail the object underlying the of use or the scheme of exemption with which Section 15C deals. The object is to benefit newly established industrial undertakings. The marginal note to which we may turn to see the drift of the section also lends support to the view which we are taking.

10. There is some difference of judicial opinion about the canon of construction applicable to a provision for exemption in a taxing statute. In *Commissioner of Income-tax Bombay v. Messrs. Chugandas and Co*[1]*.,* my brother Tendolkar and I, although we took different paths, were agreed that a provision relating td exemption must as far as possible be liberally construed and in favour of the assessee, provided in doing so no violence was being done to the language used. But in this case, as we have already mentioned, we find no difficulty in interpreting the relevant provision of the Act. If we had found any difficulty, it would have been necessary for us to bear in mind that salutary canon of construction.

11. Our answer to the question is in the affirmative.

12. Commissioner to pay the costs.

Answer in the affirmative.

[1] IT Ref. No. 27/X of 1954 (Rom)