

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

Decided on: 05.12.2016

+ **W.P.(C) 5036/2016**

LAXMI AUTOMATIC LOOM WORKS LTD.Petitioner
Through: Sh. S. Ganesh, Sr. Advocate with Ms. Suruchii
Aggarwal, Advocates.

Versus

DEPUTY COMMISSIONER OF INCOME TAX (RECOVERY)
AND ANR.Respondents
Through: Sh. D.R. Jain, Sr. Standing Counsel, for
Respondent No.1.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MS. JUSTICE DEEPA SHARMA

MR. JUSTICE S. RAVINDRA BHAT

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1. The issue that arises in the present Writ Petition is whether the benefit of exemption from Capital Gains Tax can be denied to an undertaking sought to be revived by the Board for Industrial and Financial Reconstruction (BIFR), by giving unwarranted importance and weightage to the fact that the Petitioner's net worth has turned positive without considering that the Company's carried-over losses as on 31.03.2015 amounts to ₹887.23 lakhs and the fact that it has to create Capital Redemption Reserve of ₹850 lakhs out of profits for redemption of 6% cumulative redeemable preference shares due by year 2018-19, i.e. in the three years following 2014-15.
2. The petitioner, which is engaged in textile machinery manufacture, became sick in 2001, and its case was referred to the BIFR as Case No.225

of 2001. On 19.09.2003, the scheme for revival of the Petitioner was sanctioned by BIFR. The BIFR appointed Indian Bank as monitoring agency to monitor the progress of implementation of the sanctioned Scheme. In terms of the viability projected in the sanctioned scheme of 2003, the net-worth of the company was expected to turn positive by 2005-06 and its accumulated losses were expected to be eliminated during 2006. These projections remained unfulfilled, however, and there was a sharp decrease in the company's net-worth due to which it could not generate the necessary internal accruals. The Petitioner contends that this was inasmuch as it could not take any positive steps for the sale of its assets, as contemplated in the scheme of 2003; and it could also not reach an amicable settlement with the Employees' Union in respect of BIFR's package and the terms of voluntary retirement; it could also not dispose of its surplus assets and generate the requisite amount of funds for effective revival. The BIFR, therefore, reviewed and modified the rehabilitation scheme by an order passed on 18.02.2009. The petitioner then approached BIFR through an application, requesting it to direct the income tax authorities to *inter-alia*, exempt the company from capital gains tax on the sale of assets, which was to be made by the Petitioner as part of the Modified Rehabilitation Scheme. On 09.11.2009, BIFR passed an order allowing that application. It directed the Directorate of Income Tax (Recovery) to consider the Petitioner company's request for exemption from payment of capital gains tax on the sale of assets. In the BIFR's proceedings/order dated 09.11.2009 a new Para 10.7 was included in Modified Scheme 2009, as quoted below:

"The Board on consideration of the material on record and also the submissions made noted that although the Bench passed an order

directing DIT (RECOVERY) to consider granting extension of the time for set off the carry forward losses upto 31.03.2013 and also consider exempting the Company from capital gains tax on sale of the assets, the said Clause has not been included in MS09. The Bench therefore directed that a new para as para 10.7 be inserted in MS09 to read as under:

"Para 10.7 Directorate of Income Tax (RECOVERY)

(1) To consider to grant extension of time for set off the carry forward losses upto 31-03-2013 as against 31-03-2009.

(2) To consider to exempt the company from Capital gains tax on sale of assets"

3. This order was made after hearing the advocate appearing for the DIT (Recovery). The petitioner highlights that the DIT (Recovery) had no grievance against the said direction of the BIFR dated 09.11.2009 and, therefore, did not prefer any appeal against the said direction, but allowed the same to become final. The DIT (Recovery), therefore, clearly accepted the position that if the facts and circumstances warranted, the Petitioner company would be entitled to exemption from capital gains tax in respect of assets transferred by it and such exemption should be granted to it. Further to the direction of BIFR, the Joint Director of Income Tax (Recovery) passed an order dated 29.11.2012 rejecting the request for exemption from capital gains tax. This order was passed on the basis of certain projected figures relating to the petitioner's expected profits in future years. The Petitioner then filed a writ petition, being W.P.(C) 4367/2013 before this Court challenging the legality and validity of the said order of the Joint Director dated 29.11.2012. Since the return of income for the AY 2010-11 was due by 15.10.2010, the Petitioner, pending the receipt of the order of the DIT (Recovery) filed its return of income for the AY 2010-11 on 22.09.2010

without subjecting the capital gains to tax based on the sanctioned scheme, recommending the relief of capital gains tax as well as the sanctioned scheme. The assessment order passed in the Petitioner's case for the A.Y. 2010-11 dated 08.02.2013 did not include the capital gain arising from transfer of the assets. It was, therefore, not necessary for the Petitioner Company to get the benefit of exemption from the capital gains tax. This was brought to the notice of this Court on behalf of the DIT (Recovery) and accordingly, the Petitioner's said Writ Petition No.4367/2013 was disposed of as infructuous, as it was not necessary to consider the request for grant of exemption on capital gains arising from the transfer of assets under the scheme. The order of this Court, disposing of the writ petition is as follows:

"It is stated that the Assessing Officer accepted the Petitioner's contention. The learned counsel for Petitioner states that in the circumstances there is no surviving grievance and seeks liberty to approach the Court in case the authority pass any adverse orders subsequently. Liberty granted. The Petition is dismissed as infructuous."

4. The order made by the income tax authorities after disposal of the writ petition again denied relief to the petitioner, based on an appreciation of the record and that the figures shown did not justify waiver of capital gains tax. This order was again challenged, in W.P.(C) 1568/2015, which was disposed of on 15 February 2016 in terms of the following order:

"Learned counsel for the Respondents has not been able to substantiate the plea that if there is any difference between the projections and the actuals to the detriment of the proposer, that would have to be absorbed by the proposer. Learned counsel for the Respondents drew the attention of the Court to the order passed by the Appellate Authority for Industrial and Financial Reconstruction

('AAIFR'). That order requires the Income Tax Department to accept or reject the plea for grant of a concession or relief in terms of the Scheme presented before the BIFR. The AAIFR observed that "the Department should have only considered the proposed concession and taken its own decision." That order does not by any means suggest that when there are actual figures available at the time of the decision to be taken by the Department, reliance can be placed on the projections of the Petitioner which were submitted at the time of submission of the scheme before the BIFR. In any event, it does not support the plea of the Revenue that the difference between the actuals and the projected figures should be absorbed by the Petitioner.

3. Consequently, while setting aside the order dated 29th November 2012 W.P(C) No. 1568/2015 passed by the Directorate of Income Tax ('DIT') Recovery, the Court requires the DIT (Recovery) to once again consider the proposed scheme and the question of entitlement of the Petitioner to concession as sought for by the Petitioner. A fresh decision based on the actual figures submitted by the Petitioner will be taken. It is open to the Department to elicit all the necessary information that is required by from the Petitioner in a time bound manner and take a fresh decision not later than eight weeks from today. If the Petitioner makes a request in that regard, a hearing will also be afforded to the Petitioner before the decision is taken."

5. The Income Tax authorities issued notice to the petitioner and after considering the materials furnished to them as well as the submissions made in this context, rejected the request vis-à-vis capital gains exemption, through the impugned order of 19.04.2016. The said impugned order reads as follows:

"7. In compliance with the direction of Hon'ble High Court, the Directorate sent a letter dated 02-03-2016 giving opportunity to the company to file documents/ submissions either in writing and/or in person, The company filed its replies vide letters dated 26-02-2016, 04-03-2016, 07-03-2016 (letter dated 07-03-2016 was filed by the

company's representative in person on 09-03-2016) and 10-03-2016 enclosing therewith, copies of the comparative statements of projected and actual balance sheets, details of income, surplus cash, returns filed etc. Company has also stated that its actual performance for the period F.Y.. 2008-09 to F.Y. 2012-13 is much lower (actual sales/ other income/ cash accruals less than 50% of the projected figures) than the projections shown in the sanctioned scheme.

8. Replies filed by the company as well as the information received from field authorities earlier through letter dated 11-12-2015 and other information available on record have been considered earlier, All the actual financial results, wherever available, have been taken into consideration.

9. It is noted that:

9.1 The actual figures of actual sales/ other income/ cash accruals are less than 50% of the projected figures shown in the modified rehabilitation scheme as sanctioned by the Hon'ble BIFR. However, it is the company which is solely and wholly responsible for such a situation, Income Tax Department has neither levied any tax nor took any other action against the company during this period and therefore, cannot be blamed for such a situation/poor performance of the company: It is also noted that such poor implementation of the scheme was also not brought to the notice of BIFR by the company. It is therefore clear that company's stand seeking relief on the ground of achievement of poor results by it by more than 50% of the projected figures is not tenable legally as well as technically. It is a settled principle that one cannot be given benefit of one's own default.

9.2 It is further noted that the actual figures i.e. upto F.Y. 2014-15, financials for which have been audited adopted and income tax returns filed, were not furnished by the company and were obtained from the field authorities. A perusal of these shows that the company is running very well in all respects, operational as well as financial. As on 31.02.2015, company is having huge surplus cash/fund flow, Company has also failed to show that any tax has been levied/leviable on it in respect of said capital gain. Still, however, tax

on capital gain, if at all leviable, is much below the surplus cash available with the company, payment of which is not going to affect it adversely as even after payment of such tax, company will be left with substantial surplus funds available with it.

9.3 Thus, the legal/actual/factual position shows that the company cannot be said to be in need of any relief from the Income Tax Department and it can very well survive without grant of any Income Tax relief. In fact, the company has already attained an advanced stage of its revival and there is no need to exempt the Capital Gain Tax liability at all because it will be against public interest to grant such exemption of tax liability.

Accordingly, relief relating to Capital Gain tax has not been granted to the company.”

6. The petitioner contends and its senior Counsel, Mr. S. Ganesh, argues that the fact that the Petitioner Company's net-worth has become positive only indicates that its total assets are in excess of its liabilities. The Deputy Director, however, completely failed to appreciate that even though there was a small excess of assets over liabilities, nevertheless, there was a huge amount of accumulated losses of ₹1,773,79 lakhs as on 31.03.2010, which had not been made good; and this fact by itself warranted and required the grant of exemption from capital gains tax to the Petitioner. Mr. Ganesh further argues that the impugned order does not consider the financial and liquidity strain, which the Petitioner Company would be subjected to, if the Petitioner was compelled to pay the amount of capital gains tax. It is submitted that, having regard to the fact that this is the third round of litigation, no purpose whatsoever would be served in merely setting aside the impugned order and remanding the matter for fresh consideration and for the passing of a *de-novo* order. It is submitted that, having regard to the

indisputable facts and figures on record and the fact that this is the third round of litigation, the interests of justice require that this Court to issue a writ and order directing the Respondents to grant the benefit of capital gains tax exemption to the Petitioner.

7. It is argued that the impugned order failed to consider that the Petitioner Company's carried over losses as on 31.03.2015 remain at ₹887.23 lakhs and the net worth though has become positive as on 31.03.2010, the Company has not wiped out its losses fully as on 31.03.2015. The Company is required to create Capital Redemption Reserves of ₹ 850 Lakhs to redeem its 6% Cumulative Redeemable Preferences Share of ₹100/- each in February 2020. It is stated that no funds outflow was sanctioned in the Modified sanctioned scheme in view of the capital gains tax waiver contemplated. The capital gains tax liability of ₹331.68 lakhs would substantially imperil the financial health of the petitioner and push it into an uncontrollable spiral of indebtedness from which it would lapse into sickness. It is argued that the BIFR scheme did not envision the denial of capital gains tax waiver or exemption; that was integral to the modified scheme. In fact, the assets sold (for which capital gains tax liabilities arose) were for the satisfaction of the company's other liabilities and to place it in the direction of financial recovery. The denial of the requested exemption is neither in the interests of the company, nor for that matter, in the interests of the revenue, because the alternative, i.e payment would result in bankrupting the company, deprivation of employment and deprivation of future revenues that would accrue as taxes.

8. It is argued on behalf of the revenue that the profitability of the company has been steadily on the rise; it is submitted, in this context that the

total income reported (before setting-off unabsorbed depreciation and losses) was: ₹92,47,346 for 2013-14; ₹2,70,03,675 and ₹ 3,57,74,160 for 2015-16. It is highlighted that the Audited Accounts for the F.Y. 2014-15 showed that the Petitioner Company had surplus cash of ₹670.0 lakhs as on 31-03-2015. As the payment of the tax liability on Capital Gains, if any, was to be made in the Current Year i.e. F.Y. 2016-17 only and the financial position of the Petitioner Company showed enough strength and capacity to absorb the Capital Gain Tax liability, the relief on account thereof was not allowed. The figures of Income, surplus cash and current assets as culled out from the Audited Accounts for the F. Y. 2013-14 and 2014-15 obtained from the Assessing Officer reinforced this conclusion. It is argued that on going through the returns of income and Audited Accounts of the petitioner company for the F.Y. 2011-12 onwards, it was found that the petitioner company was earning huge profits and was out of sickness. As such, there was no need to grant any tax exemption to the petitioner company. Therefore, the respondent department, in compliance of this court's order dated 15.02.2016, passed the fresh impugned order dated 19.04.2016 holding that as the petitioner company was earning huge profits, it should be able to pay the tax liability arising on capital gain income and that, therefore, it was not entitled to any tax exemptions reliefs.

9. Section 32 of the Sick Industrial Companies (Special Provisions) Act, 1985 [hereafter "the Act" which provides for the rehabilitation of sick companies under orders of the BIFR], clearly states that any direction issued by that authority would have an overriding effect notwithstanding any other provision or any law with a few exceptions. In the present case, para 17(i) (c)

of the BIFR's order requested the Director of Income (Recovery) to consider granting extension of time for set-off of carry forward losses up to 31.03.2013 as against 31.03.2009. In addition, the said Director of Income Tax (Recovery) was "*requested to consider to exempt the company from capital gains tax on sale of assets.*" The previous history of this case would show that the income tax authorities by two separate orders made on 05.09.2012 and 29.11.2012 rejected the request for waiver of capital gains tax. The previous orders, especially the order made after the first remand (dated 29.11.2012) noticed carry forward or brought forward business loss to the tune of ₹19.58 crores relating to AY 1998-99 to 2011-12. The projected profit of the assessment year in the rehabilitation period, i.e. AY 2009-10 to 2013-14 amounted to ₹29.34 crores. The respondent revenue permitted stay of brought forward business losses against the projected profit for 8 years and allowed set-off of balance forward business losses of ₹5.48 crores, i.e. ₹19.58 crores (-) Rs.14.09 crores of AY 2009-10 and 2011-12 within the normal period of three years. The order of the Joint Director of Income Tax, however, denied the relief in respect of capital gains tax on the ground that it could be set-off of against unabsorbed depreciation so that the respondent's fear of unviability in the event of outgoing of tax could be addressed.

10. This Court's order of 15.02.2016 directed the Director of Income Tax to consider the proposed claim and the question of petitioner's entitlement to concession on the basis of the actual submission figures submitted by it. The income tax authorities were at liberty to elicit all necessary fresh figures and documents in this regard. The impugned order is premised on the opinion that the actual sales and other cash accruals were less than 50% of the projected figures, within the figures projected in the rehabilitation scheme.

The order also notes that this was on account of the assessee petitioner's own functioning and for which revenue could not be blamed or faulted. The order also noted that actual figures up to FY 2014-15, financials of which were audited and adopted were not furnished by the company but were obtained by the field authorities. The order notes further that these figures show that the company has huge surplus funds and flow. The petitioner urged in this regard that even though facially the funds flow appears to be convertible and profits are on the rise, yet, having regard to the preference share liability, if the capital gains tax is insisted, not only the profitability would be wiped-out but the company might become sick. The petitioner also has placed on record the annual report for 2014-15 in support of its argument that it has large component of liability, i.e. claims for refund of security deposit and further liability of ₹8.5 crores towards the 6% cumulative redeemable preference shares. Section 32 of the Act confers primacy upon the orders of BIFR. In the present case, the BIFR directed income authorities to consider granting relief on two aspects – carry forward business losses and their absorption having regard to projected profits in terms of the modified rehabilitation scheme. That relief has concededly been granted; it is a substantial one to the extent of ₹14.09 crores. The question, therefore, is whether the income authority's refusal to grant relief on the basis of the actual figures of profitability in the circumstances of the case is warranted.

11. This Court notices that though the modified scheme was issued in 2009, the consideration and grant of relief took place on 29.12.2012 by the income tax authorities when they actually took note of the projections. It is a matter of record that the company achieved net worth and had in fact moved out of the rehabilitation phase in 2011. That was the *rationale* for this

Court's decision on 15.02.2016 that those actual figures should be taken note of. It is here that the company's functioning became material. The income tax authorities now feel that whilst the decision of carry forward was justified, the figures now based upon the functioning after rehabilitation reveal a different story, i.e. that the company has funds and that there was less than half the projected profits for a certain period having regard to the modified scheme. Now, as far as the later aspect is concerned, the income tax authority's view cannot be faulted. It is based upon objective assessment of materials on record. As to the other aspect, i.e. that the company is in possession of funds and as of late, shown profitability, the Court has in the previous part of its judgment noted that profitability has indeed been on the increase. In these circumstances, the question is whether rejection of request for exemption from payment of central government taxes (of ₹3.31 crores), is justified or an arbitrary one. There is no denial of the fact that the company has shown profitability. Its liability to redeem the preference shares is in the future. In the circumstances, the possibility of its incurring losses in the event of payment of capital gains tax cannot be ruled out. That such losses might arise could also be within the normal course of any normal business enterprise's functioning. In the circumstances, the view of the respondents that exemption from payment of capital gains tax is not warranted cannot be held illegal.

12. The Court is aware, at the same time that in the assessments completed till date, the petitioner's liability had not in one sense been crystallized. The remand to the income tax authorities on three occasions led to fresh orders based upon fresh assessment of the facts and circumstances on each occasion. Having regard to these peculiar facts, a direction is issued

to the respondents not to charge interest or penalty on the capital gains tax amounts in the circumstances of the case for the duration that the matter remained pending in these proceedings and all prior proceedings.

13. The writ petition is allowed in terms of the directions in the preceding paragraph even while upholding the liability to pay capital gains tax. No costs.

**S. RAVINDRA BHAT
(JUDGE)**

**DEEPA SHARMA
(JUDGE)**

DECEMBER 5, 2016

