

STATE OF KARNATAKA AND ANR
v.
SHREYAS PAPERS PVT. LTD. AND ORS

A

JANUARY 5, 2006

[RUMA PAL AND B.N. SRIKRISHNA, JJ.]

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Karnataka Sales Tax Act, 1957:

Section 15—Purchaser-transferee of assets of defaulting Company—transferor, if liable for sales tax arrears of defaulting Company—Held: Section 15(1) operates only when there is complete transfer of ownership of business—Defaulting Company not sold as a going concern but there was transfer of individual assets of the Company, thus, section 15 not attracted and transferee not liable for transferor's sales tax liabilities—State Financial Corporation Act, 1951—Section 29.

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Section 13(2)(i)—Creation of charge over properties of defaulter—Charge, enforcement of, against purchaser-transferee of property—Held: Transferee was purchaser for value without notice of sales tax arrears of defaulting Company or consequent charge on property—Thus, transferee held property free of charge and not liable for tax arrears of defaulting Company—Further, State Financial Corporation as transferee of assets not liable for charge created since no such issue raised or argued before High Court—Transfer of Property Act, 1882—Section 100—State Financial Corporation Act, 1951—Section 29.

E

Practice and Procedure: New relief—Permissibility of—Neither raised nor argued before, or decided by High Court—Held: It cannot be claimed before this Court unless exceptional circumstances occur—Constitution of India, 1950—Article 136.

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Karnataka State Industrial Investment and Development Corporation—second respondent granted loan to a Company. However, the Company defaulted in its repayment. Corporation then took over the assets viz., land, building, plant and machinery of the defaulting Company and advertised it for sale. First respondent purchased the assets excluding any statutory liabilities. Charge was created on the properties of the defaulting

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A Company since they defaulted in payment of sales tax. Second appellant-recovery officer issued notice under section 15 of Karnataka Sales tax Act, 1957 to first respondent to discharge sales tax arrears of defaulting Company. First respondent filed writ petition challenging the notice. High Court held that since only land, building, plant and machinery had been transferred, there was no transfer of the ownership of business of the defaulting Company, as such section 15 was not applicable to first respondent and he was not liable to pay sales tax arrears of the Company. Hence the present appeals.

C Appellant contended that the business of the defaulting Company had been transferred to the first respondent, as such the sales tax dues of the defaulting Company could rightfully be claimed and recovered from the first respondent; that since a charge over the properties of the defaulting Company had been created under the KST Act, the first respondent as the transferee held the properties subject to the charge; and that in any event, the Corporation as the transferee of the assets, by virtue of the provisions of Section 29 of the State Financial Corporation Act, would be liable to the extent of the charge created on the assets transferred.

Dismissing the appeals, the Court

E HELD: 1.1. A careful reading of Section 15(1) of the Karnataka Sales Tax Act, 1957 shows that foisting of the liabilities of the defaulting transferor onto the transferee, would come into effect only if the “ownership of the business” is transferred. It cannot be said that the ‘business’ could not be separated from the assets of the business. Business is an activity, directed with a certain purpose, more often towards producing income or profit. Ownership of assets is merely an incident rather than a characteristic of business. Hence, the mere transfer of one or more species of assets does not necessarily bring about the transfer of the “ownership of the business” for “ownership of a business” is much wider than mere ownership of discrete or individual assets. In fact “ownership of business” is wider than the sum of the ownership of the business” constituent assets. Above all, transfer of “ownership of business” requires that the business be sold as a going concern. Therefore, Section 15(1) is intended to operate only when there is complete transfer of “ownership of business” so as to render the transferee as a successor-in-interest of the transferor. Only in such an eventuality, it makes the transferee liable for the transferor’s sales tax liabilities. [242-F-H; 243-A]

H 1.2 In the instant case, there was only transfer of individual assets

of the Defaulting Company, rather than the Defaulting Company being sold as a going concern, thus, Section 15 of the Act is not attracted and the transferee is not liable for the arrears of sales tax of the concern. A

[243-A]

Karnataka State Industrial Investment and Development Corporation Ltd. v Assistant Commissioner of Commercial Taxes, Bangalore (2001) 121 STC 520 (Karn.); Alpha Silicones v. Assistant Commercial Tax Officer (Recovery), Gulbarga and Anr., (1990) 77 STC 68 (Karn.), disapproved. [243-B-D] B

Commissioner of Income Tax v. K. H. Chambers, [1965] 2 SCR 43, relied on. [243-H] C

2.1. Section 100 of Transfer of Property Act, 1882 unambiguously indicates, a charge may not be enforced against a transferee if he/she has had no notice of the same, unless by law, the requirement of such notice has been waived. [244-D]

2.2. In the instant case, no provision of law has been cited that exempts the requirement of notice of the charge for its enforcement against a transferee who had no notice of the same. Further, it is evident from the facts of the case that the first respondent had no actual or constructive notice of the charge-sales tax arrears, prior to the transfer. First respondent was a purchaser for value without notice of the sales tax arrears of the Defaulting Company or the consequent charge on the property. Thus, the property in the hands of the first respondent was free of the charge and it is not open to the appellants to enforce the liabilities of the Defaulting Company against the first respondent. D

[245-C, F; 246-A]

Dattatreya Shanker Mote v. Anand Chitaman Dater, [1974] 2 SCC 799; Deputy Commercial Tax Officer, Thudiyalur Assessment Circle, Coimbatore and Anr v. R. K. Steels (1998) 108 STC 161 (Mad), referred to. E

[244-D; 245-H] F

Ahmedabad Municipal Corporation of the City of Ahmedabad v. Haji Abdul Gafur Haji Hussenhbai, AIR (1971) SC 1201, relied on. [244-D] G

3. It is well accepted that save for exceptional circumstances, new reliefs, not argued or claimed before the High Court, cannot be prayed for before this Court. In the instant case, only two issues, first with regard H

- A** to the validity of Section 15 of the KST Act and the other with regard to the liability of the first respondent for the charge created on the properties of the defaulting company, were raised in the writ petition and seem to have argued before the High Court and dealt by it. No issue as to the liability of the Corporation was raised or argued before, or decided by High Court. In these circumstances, this Court cannot enter into the said issue and it is left open to be sorted out between appellants and second respondent in any appropriate proceedings.

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos. 3170-3173 of 2000.

- C** From the Judgment and Order dated 22.9.1999 of the Karnataka High Court in W.P. Nos. 32428/93 C/w 14332/98 and 14442-43/98.

Sanjay R. Hegde, Anil K. Mishra, A.K. Mishra and A. Rohen Singh for the Appellants.

- D** L.N. Rao, N.D.B. Raju, Ms. Bharathi, R. Goodwill Indeevar, Guntur Prabhakar, L.N. Rao, Naveen R. Nath, Ms. Lalit Mohini Bhat, Ms. Anitha Shenoy and Ms. Hetu Arora for the Respondents.

The Judgment of the Court was delivered by

- E** **SRIKRISHNA, J.** There are three questions of law to be decided in these appeals:

- F** Firstly, whether the purchaser of assets of a concern sold by a State Financial Corporation, in exercise of its powers under Section 29 of the State Financial Corporations Act, 1951 (hereinafter “the SFC Act”), would be liable under the Karnataka Sales Tax, 1957 (hereinafter “the KST Act”), for the arrears of sales tax of the concern whose assets have been transferred?

Secondly, under what circumstances does a charge created on a property become unenforceable against a transferee of such a property?

- G** Finally, whether a completely novel relief, not argued/claimed before the High Court or decided by the impugned judgment, may be claimed before this Court?

The Facts in Civil Appeal 3170/2000

- H** A company by name Mishal Paper Mills (P) Ltd. (hereinafter “the

Defaulting Company”), was running a medium-scale duplex board manufacturing unit. The Second Respondent, Karnataka State Industrial Investment & Development Corporation Ltd. (hereinafter “the Corporation”), had extended financial assistance to the Defaulting Company. However, the Defaulting Company defaulted in repayment of the loans granted to it by the Corporation. Acting under the provisions of Section 29(1) of the SFC Act, the Corporation took over the assets of the Defaulting Company. On 17.3.1992, the Corporation advertised the sale of the “assets” of the Defaulting Company i.e. the land, building, plant and machinery. In response to the advertisement, and after several rounds of negotiations, Shreyas Papers (P) Ltd. (hereinafter “the First Respondent”) entered into an agreement with the Corporation for purchase of the land, building, plant and machinery of the Defaulting Company, which was put up for sale. In Clause (2) of the offer to purchase (dated 5.6.1992), the First Respondent specifically stated:

“We shall be taking over the unit with ‘zero’ liabilities and shall not be held responsible for any existing statutory liabilities of the above said unit like Sale Tax, Excise Duty, Municipal taxes, E.S.I. and P.F. development loan, Central and State subsidy and rank liabilities etc. except as agreed in the meeting for KEB. and labour dues.”

This offer was accepted by the Corporation and the sale took place consequent thereto.

On 8.1.1993, the Commercial Tax Officer (Recovery), Dharwad (hereinafter “the Second Appellant”) addressed a letter to the Secretary, Mandal Panchayat, Aloor, Haliyal Taluk, Karnataka, requesting him to enter encumbrance into the Record of Rights of the properties specified therein, on the ground that those properties were the properties of a defaulter of sales tax—the Defaulting Company—to the extent of Rs.21,79,715. The First Respondent wrote a letter (dated 31.5.1993) to the Corporation thereby requesting that a letter be addressed to the Second Appellant to withdraw his letter dated 8.1.1993, as the Corporation was the first charge holder and the assets had been sold to it by the Corporation free of all charges. A letter was addressed, as requested, on 5.7.1993 by the Corporation to the Second Appellant. On 11.8.1993, the Second Appellant issued a notice under Section 15 of the KST Act informing the First Respondent that a charge had been created on the properties of the Defaulting Company on 17.2.1992 as the latter had defaulted in payment of sales tax. It also noted that the assets of the Defaulting Company had been transferred from the Corporation to the

A First Respondent on 12.8.1992. It was further stated that the First Respondent being the transferee of the business, was jointly liable to discharge the arrears of sales tax of the Defaulting Company by virtue of Section 15(1) of the KST Act.

B As the sales tax authorities were not willing to relent, the First Respondent moved a Writ Petition No. 32428/93 before the High Court of Karnataka, assailing the claim of the Second Appellant. The substantive reliefs claimed therein were two fold:

“(A) Declare that the provisions of Section 15 of the Karnataka Sales Tax Act are void;

C (B) Issue a writ of mandamus or any other appropriate writ or order or direction restraining the respondents 1 and 2 not to take any action against the petitioner for the recovery of the alleged sales tax recovery as mentioned in the communication No. RRY.CR.3.92-93.1168 dated 11.8.1993...”

D By a common judgment (dated 22.9.1999)¹ rendered in four similar writ petitions, the High Court of Karnataka allowed the writ petition. The High Court held that the petitioner, being the purchaser in the auction from the Corporation, only of the land, building, plant and machinery, could not be considered as the transferee of the ownership of the business of the

E Defaulting Company. The High Court found that although land, buildings, plant and machinery of the Defaulting Company had been transferred to the First Respondent, since the goodwill of the business had not been transferred, there was no transfer of the ownership of the business. On this reasoning, the High Court took the view that Section 15 of the KST Act would not apply

F to the First Respondent and consequently that the First Respondent was not liable for the sales tax arrears of the Defaulting Company. Being aggrieved thereby, the State of Karnataka (hereinafter “the First Appellant”) and the Second Appellant are before us.

The Appellant's Contentions

G Mr. Hegde, learned counsel for the appellants, made three broad submissions: Firstly, he placed heavy reliance on certain relevant provisions of the KST Act, and contended that the High Court had completely

H ¹Reported in: *Shreyas Papers Pvt. Ltd v. State of Karnataka* (2001) 121 STC 94 Karn.

misunderstood the import of these sections. He urged that upon a true interpretation of the provisions of the KST Act, particularly Sections 13 and 15 read with Section 2(f-2), it would be clear that the First Respondent was the entity to whom the business of the Defaulting Company had been transferred. Therefore, Mr. Hegde urged, the sales tax dues of the Defaulting Company could rightfully be claimed and recovered from the First Respondent.

Secondly, Mr. Hegde submitted that since a charge over the properties of the Defaulting Company had been created under the KST Act, the First Respondent as the transferee held the properties subject to the charge.

Finally, and as an alternative submission, Mr. Hegde contended that, merely because the Corporation had acted in exercise of its power under Section 29 of the SFC Act, it did not get any priority over the dues of the State. Therefore, he argued, the Corporation was liable to make good the amount of sales tax arrears of the Defaulting Company, at least to the extent of the sale proceeds of the assets of the Defaulting Company.

Transfer of "Ownership of Business" under Section 15 of the KST Act

To determine whether the First Respondent is liable for sales tax arrears of the Defaulting Company, a survey of the applicable provisions in the SFC Act and KST Act becomes necessary.

Section 2(f-2) of the KST Act defines the expression "business" in an inclusive manner and provides that activities of different nature, as contemplated in sub-sections (i) and (ii), would be included within the definition of the expression. Section 13(2)(i) of the KST Act provides that if a default is made in making payment of sales tax, then:

"...the whole of the amount outstanding on the date of default shall become immediately due and shall be a charge on the properties of the person or persons liable to pay the tax or any other amount due under this Act."

Section 15(1) of the KST Act provides:

"When the ownership of the business of a dealer liable to pay the tax or penalty, or any other amount under the provisions of this Act, is transferred, the transferor and the transferee shall jointly and severally be liable to pay any tax or penalty or any other amount payable in respect of such business and remaining unpaid at the time of transfer,

A and for the purpose of recovery from the transferee such transferee shall be deemed to be the dealer liable to pay the tax or penalty or other amount under this Act.”

B Section 29 of the SFC Act gives an extraordinary power to the Corporation. It provides that in the event of a borrower making a default in its obligations towards repayment or in relation to any guarantee, then the Corporation:

C “...shall have the right to take over the management or possession or both of the industrial concerns, as well as the right to transfer by way of lease or sale and realise the property pledged, mortgaged, hypothecated or assigned to the Financial Corporation.”

Sub-section (2) of Section 29 provides that:

D “Any transfer of property made by the Financial Corporation, in exercise of its powers under sub-section (1), shall vest in the transferee all rights in or to the property transferred as if the transfer had been made by the owner of the property.”

Finally, sub-section (5) of this Section provides:

E “Where the Financial Corporation has taken any action against an industrial concern under the provisions of sub-section (1), the Financial Corporation shall be deemed to be the owner of such concern, for the purposes of suits by or against the concern, and shall sue and be sued in the name of the concern.”

F A careful reading of Section 15(1) of the KST Act shows that the consequences contemplated therein, namely, foisting of the liabilities of the defaulting transferor onto the transferee, would come into effect only if the “ownership of the business” is transferred. Although, Mr. Hegde strenuously urged that “business” could not be separated from the assets of the business, we are unable to accept this contention. Business is an activity, directed with a certain purpose, more often towards producing income or profit. Ownership of assets is merely an incident rather than a characteristic of business. Hence, the mere transfer of one or more species of assets does not necessarily bring about the transfer of the “ownership of the business” for “ownership of a business” is much wider than mere ownership of discrete or individual assets. In fact, “ownership of business” is wider than the sum of the ownership of H a business’ constituent assets. Above all, transfer of “ownership of business”

requires that the business be sold as a going concern.² In our view, therefore, Section 15(1) is intended to operate only when there is complete transfer of “ownership of business” so as to render the transferee as a successor-in-interest of the transferor. Only in such an eventuality does Section 15(1) make the transferee liable for the transferor’s sales tax liabilities. A

Mr. Hegde referred to two judgments of the Karnataka High Court both of which, unfortunately, take an erroneous view of the matter. In Karnataka State Industrial Investment and *Development Corporation Ltd. v. Assistant Commissioner of Commercial Taxes, Bangalore*,³ the High Court held that when Section 29 of the SFC Act was read with Section 15 of the KST Act, the transferee would be jointly liable with the State Finance Corporation concerned. As we have already held, Section 15 operates only in a situation where the ownership of the business is transferred. The learned Single Judge, however, did not notice this point. Similarly, we are unable to accept the correctness of the judgment in *Alpha Silicones v. Assistant Commercial Tax Officer (Recovery), Gulbarga and Anr.*⁴ as it held that even the mere transfer of assets would amount to transfer of ownership of the business. We overrule these two judgments to the extent that they conflict with the views expressed herein. B C D

In the present case, since it is not a matter of dispute that there was only the transfer of individual assets of the Defaulting Company, rather than the Defaulting Company being sold as a going concern, in light of our expressed views, Section 15 of the KST Act is not attracted. The first limb of Mr. Hegde’s arguments must, therefore, fail. E

Enforceability of the Charge

The next limb of Mr. Hegde’s arguments was that since Section 13(2)(i) of the KST Act creates a charge on the property of the Defaulting Company, the charge would continue on the properties, even if it changes hands by transfer. F

While the expression “charge” is not defined by the KST Act, this concept is well known in property law and has been defined by Section 100 of the Transfer of Property Act, 1882 (hereinafter “the TP Act”). Here “charge” G

²*Commissioner of Income Tax v. K.H. Chambers*, [1965] 2 SCR 43 at p.49

³(2001) 121 STC 520 Karn.

⁴(1990) 77 STC 68 Karn. H

A is defined as:

“Where immoveable property of one person is by act of parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property; and all the provisions hereinbefore contained which apply to a simple mortgage shall, so far as may be, apply to such charge.

B Nothing in this section applies to the charge of a trustee on the trust-property for expenses properly incurred in the execution of his trust, and, *save as otherwise expressly provided by any law for the time being in force, no charge shall be enforced against any property in the hands of a person to whom such property has been transferred for consideration and without notice of the charge.*” (emphasis supplied)

C As the section itself unambiguously indicates, a charge may not be enforced against a transferee if s/he has had no notice of the same, unless by law, the requirement of such notice has been waived. This position has long been accepted by this Court in *Dattatreya Shanker Mote v. Anand Chitaman Datar*,⁵ and in *Ahmedabad Municipal Corporation of the City of Ahmedabad v. Haji Abdul Gafur Haji Hussenhaji*⁶ (hereinafter “Ahmedabad Municipal Corporation”). In this connection, we may refer to the latter judgment, which is particularly relevant for the present case.

D *Ahmedabad Municipal Corporation* was a case where a person was in arrears of property tax, due under the Bombay Provincial Municipal Corporation Act, 1949. Consequently, the Municipal Corporation created a charge over the property of the defaulter. However, the property was sold in execution of a mortgage decree. When the Municipal Corporation purported to exercise their charge over the property, the purchaser in court auction filed a suit for a declaration that he was the owner of the property and that the arrears of municipal taxes due by the transferor were not recoverable from him by proceeding against the property purchased in auction. In the appeal before this Court, the Municipal Corporation’s main argument was that where the local law provided for the creation of a charge against a property for

⁵[1974] 2 SCC 799 at p. 811 (paragraph 18).

H ⁶AIR (1971) SC 1201 at pp. 1202-1204 (paragraph 3.)

which municipal taxes were due, transferees of such properties were imputed with constructive knowledge of any charge created against the properties that they had purchased. This argument was, however, rejected. This Court held that while constructive notice was sufficient to satisfy the requirement of notice in the proviso to Section 100 of the TP Act, whether the transferee had constructive notice of the charge had to be determined on the facts and circumstances of the case.⁷ In other words, this Court held that there could be no fixed presumption as to the transferee having constructive notice of the charge against the property. In fact, the principle laid down in *Ahmedabad Municipal Corporation* has been correctly applied in a sales tax case similar to the present case.⁸

In the present case, firstly, no provision of law has been cited before us that exempts the requirement of notice of the charge for its enforcement against a transferee who had no notice of the same. It remains to be seen, therefore, if in the facts of the present case, the First Respondent had notice-actual or constructive-of the charge. At the outset, in the advertisement/notice dated 17.3.1992 issued by the Corporation, mention is only made of the sale of the Defaulting Company's assets and there is no indication, whatsoever, of any sales tax arrears. Further, the bid offer made on behalf of the First Respondent on 5.6.1992 specifically excludes any statutory liabilities, including sales tax. This offer was accepted by the Corporation on 15.7.1992. Even at that stage, there was no mention of any sales tax arrears. The sale of the assets took place pursuant to the agreement dated 12.8.1992 in which a specific clause was inserted that the First Respondent would be liable to pay all property taxes, other taxes, electricity bills, water taxes and rents from the date of the agreement (i.e. 12.8.1992). For the first time, by letter dated 8.1.1993 of the Second Appellant to the Mandal Panchayath, Aloor Taluk, the issue of sales tax dues of the Defaulting Company was brought to the surface. This is further borne out by the correspondence between the First Respondent and the Corporation. Thus, it is evident that the First Respondent had no actual notice of the charge prior to the transfer. As to whether the First Respondent had constructive notice of the charge, no substantive argument on this issue was made, either before the High Court or at any rate before us. Hence, we cannot hold that the First Appellant had constructive notice of the

⁷ Ibid at pp. 1207-1208 (paragraph 8.)

⁸ *Deputy Commercial Tax Officer, Thudiyalur Assessment Circle, Coimbatore and Anr. v. R.K. Steels.* (1998) 108 STC 161 Mad.

A charge.

In these circumstances, we are of the view that the First Respondent was a purchaser for value without notice of the sales tax arrears of the Defaulting Company or the consequent charge on the property. This would, therefore, attract the principle laid down by this Court in *Ahmedabad Municipal Corporation*, which is also embodied in the proviso to Section 100 of the TP Act. Thus, the property in the hands of the First Respondent was free of the charge and it is not open to the appellants to enforce the liabilities of the Defaulting Company in this manner against the First Respondent.

C *The Liability of the State Financial Corporation*

Mr. Hegde then turned to his final argument that, in any event, the Corporation as the transferee of the assets, by virtue of the provisions of Section 29 of the SFC Act, would be liable to the extent of the charge created on the assets transferred.

D In our view, it is not necessary for us to go into this question. As we have pointed out at the commencement, only two issues were raised in the writ petition and seem to have been argued before the High Court: First, with regard to the validity of Section 15 of the KST, the High Court has dealt with it, and in this appeal by the State, this contention could not have been advanced. E The second issue urged before us was with regard to the liability of the First Respondent for the charge created on the properties of the Defaulting Company. The High Court, rightly in our view, held that the First Respondent before us was not liable for the tax arrears of the Defaulting Company. No issue as to the liability of the Corporation was raised or argued before, or decided by the High Court.

F It is well accepted that, save for exceptional circumstances, new reliefs, not argued or claimed before the High Court, cannot be prayed for before this Court. In these circumstances, we decline to enter into the said question, and leave it open to be sorted out between the appellants and the Second Respondent in any appropriate proceedings.

G *The Final Findings*

In light of our findings above, we find no merit in C.A. No. 3170/2000 and consequently it is dismissed.

H Civil Appeal Nos. 3171-3173/2000 pertained to the tax dues of M/s

Alpha Pharmaceuticals, which is the Second Respondent in these three appeals. A
At the stage of admission before this Court, the appeal against the Second
Respondent was dismissed. During the final arguments, Mr. Hegde, stated
that the sales tax arrears arising out of the common judgment of the High
Court of Karnataka in Writ Petition Nos. 14332/98 and 14442-43/98 have
already been recovered from the transferee concerned namely M/s Bal Pharma B
Ltd., which is the First Respondent in these appeals. Consequently, these
appeals are dismissed as infructuous.

There shall be no order as to costs.

N.J.

Appeal dismissed. C