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Tax holiday continues post merger, benefit attached to the undertaking and not to ownership

In brief

In a recent decision in the case of Shri Renuga Textiles Mills Ltd[1] (assessee), the Madras High Court (the Court) held that exemption under section 10B of the Income-tax Act, 1961 (the Act) is available to the amalgamated company (hitherto claimed by the undertaking of the amalgamating company) for the unexpired period as the exemption is attached to the undertaking and not to the ownership.

Facts

- Renuga Soft-X Towels Pvt. Ltd. (RSTL or amalgamating company) was a 100% subsidiary of the assessee and registered as a 100% export oriented unit (EOU). RSTL was claiming exemption under section 10B of the Act.
- RSTL was merged with the assessee company. After the merger, the assessee company again obtained 100% EOU recognition (with respect to the merged undertaking of RSTL) from the relevant department of the government of India.

[1] Shri Renuga Textiles Mills Ltd. *v.* CIT [TS-517-HC-2012(MAD)]

- Based on the above recognition, the assessee sought to claim exemption of income earned by its 100% EOU under section 10B of the Act for assessment year (AY) 1994-95.

- The assessing officer (AO) rejected the assessee's claim on the ground that there were no provisions for granting allowance (under section 10B of the Act) on the basis of the ownership of the new undertaking.

- The Commissioner of Income-tax (Appeals) (CIT(A)) upheld the appeal of the assessee on the grounds that:

  - Consequent to amalgamation, the EOU status passed on from the amalgamating company to the amalgamated one which was further approved by the government of India.

  - There was no violation of section 10B(2)(iii) of the Act (*which provides that exemption* under section *10B of the Act is allowed if the undertaking claiming the exemption is not formed by the transfer to it of machinery or plant previously used for any purpose*).

- The Income-tax Appellate Tribunal (the Tribunal) upheld the order of the CIT(A) on the grounds that:

  - The amalgamating company was a 100% EOU and after the amalgamation, the government of India has again recognised the status of the assessee as 100% EOU.

  - As per the Central Board of Direct Taxes (CBDT) circular no. 378 dated 3 March 1984, the relief or benefit under a tax holiday was undertaking-specific and not ownership or company-specific.

Issue

- Whether the amalgamated company is eligible for exemption under section 10B of the Act which was granted to the amalgamating company in respect of an EOU set up by it

Revenue's contentions

- On amalgamation, the amalgamating company is wound up and its entire business is transferred to the assessee's company resulting in the transfer of plant and machinery previously used by the amalgamating company to the new business (acquired after the amalgamation), by the assessee.

- As per section 10B(7A) of the Act, *in the case of amalgamation or demerger, no exemption shall be admissible for the previous year in which the amalgamation or the demerger takes place and the provisions of section 10B of the Act would apply to the amalgamated or resulting company as they would have applied to the amalgamating or demerged company if the amalgamation or the demerger had not taken place.*

  The above specific provision relating to the eligibility of exemption under section 10B of the Act to the amalgamating company after the amalgamation was introduced only with effect from 1 April 2004. It is thus not available to the assessee for AY 1994-95.

Assessee's contentions

- As per the CBDT circular no 378 dated 3 March 1984, the benefit of a tax holiday is undertaking-specific and not ownership-specific. Thus, the successor will be entitled to the benefit of the tax holiday for the unexpired period.

- There is no transfer (of plant and machinery previously used) to a new business on a merger.

- Further, as the assessee is again recognised as a 100% EOU by the government of India, it is not open to revenue authorities to dispute the assessee's claim.

High Court Ruling

- There's no denying the fact that the assessee's business is not formed by splitting up or reconstruction of business already in existence.

- Relying on the decision of the Supreme Court in the case of Saraswati Industrial Syndicate Ltd.[2], the Court held that although, post amalgamation, the amalgamating company loses its entity, no new business is formed that can be disqualified from claiming a tax holiday under section 10B of the Act.

- As per the CBDT circular dated 13 December 1963, the benefit of a tax holiday is available to the successor for the remaining period as it is attached to the undertaking and not to the owner.

- The assessee's status as 100% EOU was also approved by the government of India.

- In light of the above, it is not necessary to probe whether the provisions of section 10B(7A) of the Act which are introduced subsequent to the relevant AY would have any relevance to understand the assessee's claim.

Conclusion

The Court held that the benefit of the tax holiday is undertaking-specific and not ownership-specific. Also, post amalgamation, even though the amalgamating company loses its identity, no new business is formed that can be disqualified from claiming a tax holiday. Furthermore, the EOU status of the undertaking was also approved by the government of India. Thus, the exemption under section 10B of the Act is available to the amalgamated company.

This ruling is pertinent where the successor has acquired an undertaking availing a tax holiday pursuant to business restructuring (like amalgamation, demerger, slump sale, etc).

[2] Saraswati Industrial Syndicate Ltd. *v.* CIT [1990] 186 ITR 278(SC)

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