IN THE HIGH COURT OF JUDICATURE AT BOMBAY
O. O. C. J.

APPEAL NO.1026 OF 1997
IN
WRIT PETITION NO.2193 OF 1993

M/s. Shubham Knit Wear Pvt. Ltd.
A Company incorporated under the
Companies' Act, 1956 and having its
registered office at 142/C,
N.M. Joshi Marg, Mumbai-400 013. ....Appellant.

Vs.

1. The Regional Provident Fund
Commissioner, Maharashtra & Goa,
Bhavishya Nidhi Bhavan,
Bandra (East), Mumbai-400 051.
2. M/s. Rolex Hosiery Pvt. Ltd.,
Having its registered office at
18 Vasant Vihar C-Road,
C-Road, Churchgate, Mumbai-400 020.
3. The Union of India,
having its office at
Aaykar Bhavan, 2nd floor,
Churchgate, Mumbai-400 020. ...Respondents.

....

Shri S. C. Naidu i/b. C.R. Naidu & Co. for the Appellant.
Shri S.M. Shah for Respondent No.3.

.....

CORAM : R. M. S.KHANDEPARKAR &
DR.D.Y.CHANDRACHUD, JJ.

1st March, 2007.

JUDGMENT (PER DR. D.Y. CHANDRACHUD, J.):

a

I

An order passed by the Regional Provident Fund Commissioner holding that the establishment of the Petitioner would be considered as forming part of the establishment of the Second Respondent in terms of Section 2A of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 and denying the benefit of "infancy protection" under Section 16(1)(d) was challenged in proceedings under Article 226 of the Constitution before this Court. The petition was dismissed by a Judgment and Order of the Learned Single Judge of 19th February 1997. The correctness of the order of the Learned Single Judge has been impugned in these proceedings in appeal. The provisions of Section 2A fall for interpretation. Our conclusion, upon hearing Counsel is that the First Respondent and the Learned Single Judge are in error.

II

The Controversy:

2. The Appellant was incorporated under the Companies' Act, 1956 on 20th January 1984. The Appellant engages inter alia in the manufacture, distribution, export and supply of ready made garments. The Second Respondent was engaged in the

manufacture and sale of hosiery products including undergarments and was, at the material time, a registered proprietor in India of the Trade Mark, 'Victor'. On 1st May 1984, an agreement was entered into by the Appellant with the Second Respondent. By the provisions of the agreement, called a “licence agreement” by the parties, the Second Respondent granted to the Appellant, a licence as a registered user to the non-exclusive right to use the Trade Mark 'Victor' within the territories of the Maharashtra and Madhya Pradesh. The use of the Trade Mark was to be confined to articles listed out in Schedule B to the agreement which covered four designs of Men's undergarments. In pursuance of the registered user agreement, the Second Respondent was empowered to ensure that the goods manufactured by the Appellant fulfilled the standard of quality associated with the Trade Mark of the Second Respondent. The Second Respondent was empowered by the terms of the agreement to provide specifications of the plant and machinery to be purchased by the Appellant to conform to the process and technical advice specified by the Second Respondent and to allow the Second Respondent to inspect the manufacturing operation. Under the terms of the agreement, the Appellant agreed to pay a royalty of Rs. 1.50 per dozen in consideration of the Second Respondent imparting technical knowhow and permitting the use of the mark. In order to facilitate supervision of the quality of the goods manufactured by the Appellant, the Second Respondent had granted to the Appellant a licence to use the space situated on the premises of the Second Respondent at Lower Parel. Expenses on advertisements and publicity were to be shared by the parties. The agreement was terminable with three months' notice.

3. The agreement between the Appellant and the Second Respondent was confined to one product – men's undergarments – incorporating four designs. Apart from the aforesaid products, both the Appellant and the Second Respondent manufactured a range of products to which the agreement did not extend. At the material time, the Appellant was also engaged in the manufacture of garments under the trade name “Shabnam”. According to the Appellant, the purchase of raw material both by the Appellant and by the Second Respondent was carried out independently. The Second Respondent manufactured, marketed and distributed products manufactured under the Trade Mark, 'Victor' in various other parts of India other than the States of Maharashtra and

Madhya Pradesh which did not form part of the registered user agreement. The agreement between the Appellant and the Second Respondent did not, in other words, cover the entire scope of operation or the range activities carried out by the Appellant and the Second Respondent .

4. The Second Respondent has an establishment which is already covered by the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952, to which a Code – MH/1084 had been assigned. According to the Appellant, Section 16 of the Act, as it existed on 20th January 1984, granted "infancy protection" to an industry which was newly established. Section 16(1)(b) as it stood at the material time, was to the following effect:

> "16. **Act not to apply to certain establishments**.-
>
> (1) This Act shall not apply-
>
> (a) ....
>
> (b) to any other establishment employing fifty, or more persons or twenty or more, but less than fifty persons until the expiry of three years in the case of the former and five years in the case of the latter, from the date on which the establishment is, or has been set up."

Section 16 came to be amended with effect from 1st August 1988 by Act 33 of 1988 as a result whereof, clause (d) of sub-section (1) dealt with infancy protection to an establishment that was newly set up. Section 16(1)(d) as amended read as follows :

> "**16. Act not to apply to certain establishments.-**
>
> (1) This Act shall not apply -
>
> (a) ....
>
> (b) ....
>
> (c) ....
>
> (d) to any other establishment newly set up, until the expiry of a period of three years from the date on which such establishment is, or has been set up."

As a result of the amendment, the infancy protection under clause (d) was confined to a period of three years from the date on which the establishment was set up. Section 16(1)(d), it may now be noted, has been deleted with retrospective effect from 22nd September 1997 by Act 10 of 1998.

5. Upon incorporation on 20th January 1984, the Appellant obtained registration from diverse regulatory authorities and under various enactments, both Central and State that held the field including among them: (i) The Directorate of Industries, Maharashtra State, as a Small Scale Unit; (ii) A factory licence

under the Factories Act, 1948; (iii) Registration under the Central Sales Tax Act, 1959 and under the Central Sales Tax (Regulation and Turnover Rules, 1957; (iv) Registration under the Employees' State Insurance Act, 1948; (v) Municipal permission under the Mumbai Municipal Corporation Act, 1888; and (vi) Permission under the Maharashtra Labour Welfare Fund. The Second Respondent on its part, has a separate registration, permit and licences. The Appellant has a separate electric connection. The machinery at the premises of the Appellant was purchased, procured and installed by the Appellant and paid for by the Appellant between 20th January 1984 and 31st March 1985 at an investment of Rs.89,434/-. The plea of the Appellant is that the two establishments, at all material times, maintained separate stores and carried out their purchases independently. The Appellant maintained a separate set of employees and a separate muster roll. The conditions of service of the employees of the Appellant are stated to have been distinct from those governing the employees of the Second Respondent. The employees of one of the two organizations could not be transferred to the other. The management of the Appellant and of the Second Respondent respectively exerted no control, supervision or authority over the staff of the other. Since both the Appellant and the Second Respondent were incorporated separately, each maintained a separate Profit and Loss Account and Balance-sheet in respect of their own operations. Both the Appellant and the Second Respondent were assessed separately for the purposes of Sales Tax and Income Tax. In other words, the case as has been set up before the Court by the Appellant is that save and except the registered user agreement under which the Appellant had a non-exclusive licence to use the Trade Mark of the Second Respondent in the territories of the State of Maharashtra and Madhya Pradesh in respect of one specified product comprising of four designs against the payment of royalty, both sets of Companies maintained their independent existence. According to the Appellant, the provisions of the registered user agreement which empowered the Second Respondent to exercise supervision over the quality of the product manufactured by the Appellant were in order to ensure that the distinctiveness of the Trade Mark forming the subject matter of the agreement was not diluted. Apart from the product that was covered by the registered user agreement, the Appellant manufactured other goods. There was, according to the Appellant, therefore, no commonality of ownership or management and both

a

the Companies were independent in finance, administration and human resources.

b

6. In January 1989, the Provident Fund Inspector visited the establishment of the Appellant and according to the Appellant, advised it that the provisions of the Act were applicable to the Appellant since the infancy protection was not available to an establishment which had completed three years' of existence. The Appellant, it has been stated, computed and paid Provident Fund dues with effect from 1st August 1988. By a letter dated 28th July 1989, the Regional Provident Fund Commissioner (RPFC) directed the Second Respondent to seek compliance under the provisions of the Act in respect of the employees of the Appellant with effect from 1st May 1984. A copy of the letter having been endorsed to the Appellant, a response was submitted on 22nd August 1989 by the Appellant stating that at all material times, it was completely independent of the Second Respondent. The Appellant sought the allotment of an employees' code so as to enable it to independently comply with the provisions of the Act. While adverting to the registered user agreement, the Appellant reiterated its case that there was no commonality of ownership and

no financial or other connection between the Appellant and the Second Respondent. The Second Respondent by a letter dated 21st August 1989, similarly informed the First Respondent that it could not be called upon to pay the contribution in respect of the employees of the Appellant. On 27th December 1989, the First Respondent called upon the Appellant to seek compliance under the provisions of the Act in respect of the employees' code allotted to the Second Respondent. On 11th January 1990, the Assistant Provident Fund Commissioner informed the Second Respondent that "in continuation" of the original Code (MH 1391) allotted to the Second Respondent, a sub-code (MH-1391-A) was being allotted to the Appellant herein, on the basis that the Appellant was a branch of the Second Respondent. Accordingly, the Second Respondent was informed that "the said Branch/Head Office will be treated as one along with your main establishment."

7. Eventually, an enquiry under Section 7A of the Act was instituted by the First Respondent in the course of which, the Appellant filed several documents, among them, being the Registration Certificate under the Bombay Sales Tax Act, SSI Certificates, Factory licence, Central Sales Tax Registration,

Municipal storage licence, Income Tax and Sales Tax assessments, financial statements for the years 1985-88 and 1990-93 allegedly showing the products manufactured both under the licence and directly. The contention of the Appellant was that it was an independent, separate and distinct establishment. The Appellant claimed that it was neither producing goods for the benefit of the Second Respondent, nor did its existence depend on the Second Respondent. The licence granted by the Second Respondent was confined to only one product comprising of four designs, out of a range of products manufactured and distributed by the Appellant all over India. Moreover, it was submitted that the income from the licensed product was miniscule as compared to the sales of the products of the Appellant marketed under its Trade Mark "Shabnam". The Appellant, it was submitted, was independently registered under various statutory provisions and there was no commonality of ownership or management. The administrative affairs of the Appellant were managed independently of the Second Respondent.

8. The First Respondent passed an order on 24th May 1993 rejecting the submissions of the Appellant. The First Respondent

held that the establishment of the Appellant was a part of the main establishment of the Second Respondent and that accordingly, the provisions of the Act would be applicable to the Appellant from the date of its inception in terms of Section 2A of the Act. The First Respondent held that the establishment was not entitled to infancy protection. Thereupon by an order dated 21st October 1993, the dues payable by the Appellant were quantified at Rs.52,372.65.

9. The Appellant instituted a Writ Petition under Article 226 of the Constitution before this Court. The petition came to be dismissed by a judgment and order of the Learned Single Judge dated 19th February 1997. The Learned Single Judge held that complete control was handed over by the Second Respondent to the Petitioner, the RPFC was entitled to treat the Petitioner as a part of the Second Respondent. An adverse inference was drawn since the Second Respondent had not been served with the proceedings.

III

Submissions:

10. In assailing the findings of the Learned Single Judge

and the order of the First Respondent, it has been submitted that (i) The Appellant is not a department or branch of the Second Respondent; (ii) In any event if the Appellant were to be held to be a branch of the Second Respondent, a demand for contribution could not have been raised upon the Appellant since in that case, it would be the Second Respondent which would be an establishment within the meaning of Section 2A; (iii) The material that was produced before the First Respondent clearly demonstrated that the Appellant manufactured several products besides those for which a licence agreement was entered into with the Second Respondent; (iv) The royalty which was payable to the Second Respondent was only a miniscule proportion of the total income of the Appellant from sales; (v) Besides the product and the licence from the Second Respondent, the Appellant manufactured a substantial quantity of its own products; (vi) There was absolutely no evidence of functional integrality or material that would show that the closure of one unit of the Appellant would lead to the closure of the unit of the Second Respondent or vice versa; (vii) There was neither a common ownership or commonality of Directors or employees as between the Appellant and the Second Respondent. Consequently, it was submitted that the

a

finding in the order of the First Respondent to the effect that the Appellant is a branch of the Second Respondent was perverse and ought to have been interfered with by the Learned Single Judge in the exercise of the jurisdiction under Article 226 of the Constitution.

b

c

11. On the other hand, Counsel appearing on behalf of the First Respondent has supported the findings contained in the order of the First Respondent.

d

IV

Section 2A:

e

12. Section 2A of the Act provides as follows :

> "2A. Establishment to include all departments and branches.- For the removal of doubts, it is hereby declared that where an establishment consists of different departments or has branches, whether situate in the same place or in different places, all such departments or branches shall be treated as parts of the same establishment."

f

g

13. The aforesaid statutory provision deals with a situation where an establishment consists of different departments or where an establishment has branches, whether situated at the same place or at different places. By a deeming fiction the statute

h

provides that all such departments or branches shall be treated as part of the same establishment. The expressions “department” and “branch” have not been defined by the Act and must, therefore, bear their ordinary connotation. A branch is a division, sub-division, department or component portion of an organisation or system. A “department” is a separate division of a complex whole or one of the separate divisions or branches of State or Municipal administration. In the context of the State, a department is regarded as a division of the executive branch of Government (Law Lexicon by P. Ramanatha Aiyer, (2001) Second Edition pages 239, 522). In order to constitute a branch, an administrative unit must constitute a component of the main organisation or system. Where two units or establishments are independent – independence being defined with reference to parameters such as management, finance, supervision and administration, one cannot be regarded as a branch of the other.

Precedent :

14. In **Dharamsi Morarji Chemicals Co.Ltd. v. N.G. Desai**,[1] a Public Limited Company had established a factory in Ambarnath

1 1985 I LLJ 433

for dealing in fertilizers and subsequently, a factory at Roha for manufacturing organic chemicals. Under the infancy protection granted by Section 16(1)(d) of the Act, the provisions of the Act were not applicable to the factory at Roha for a period of three years. The management, however, restricted its entitlement to claim a benefit to a period of one year by an agreement with the employees. The RPF Commissioner denied the benefit of the exemption under Section 16 on the ground that there was commonality of ownership and management in respect of the factory at Ambarnath and Roha. A Learned Single Judge of this Court, while allowing the petition filed by the management against the order of the Provident Fund Authorities held thus:

> "As indicated, the Ambarnath factory was established as long back as in the year 1921 or thereabout while the Roha factory was established as late as July, 1977. The Ambarnath factory manufactures heavy inorganic chemicals and mainly fertilizers while the Roha factory manufactures only organic chemicals. The products manufactured at these two factories are thus separate, distinct and different. The workers of these two factories are also separate. Though at the time when the Roha factory was established or set up, about 5 to 6 employees of the Ambarnath factory were sent to Roha factory to take advantage of their expertise and experience in help set up the Roha factory this circumstance by itself has hardly any significance in deciding as to whether in law the two factories constitute one or separate establishments. In the very nature of things when a new factory is sought to be set up, the

a

benefit of such expertise and experience surely can be availed of. This by no stretch can be construed to conclude that the two factories, therefore constitute one establishment.

b

4. Other facts and circumstances also militate against the contention on behalf of the respondents that the two factories are indeed one for the purposes of the Act. Thus, the two factories have separate registration numbers. The same are also separately registered under the Factories Act. The said factories also maintain and draw up separate profit and loss accounts. The said two factories also have separate works managers and plant superintendents. And each factory also has a separate and independent set of workmen or employees who are not as such transferable from one factory to the other. The workers at the Roha factory were recruited directly from outside sources. One also does not find any supervisory control by either of these factories over the other. The two factories do not have any inter-connection as such in the matter of supervisory, financial or managerial control. Inference and conclusion is irresistible that these two factories constitute distinctly different entities and separate establishments."

c

d

e

15. The Court held that the factory at Roha was neither a branch of the factory at Ambarnath, nor its subsidiary, nor could it be termed as "a feeding factory". There was no bar, according to the Court, to a Company establishing more than one factory and the mere fact that the Company ultimately consolidated the accounts of the two factories for the purpose of the Companies Act and the Income-tax Act cannot result in the conclusion that the two

f

g

h

factories constitute one establishment. The claim of the Company to the benefit of Section 16 qua the Roha factory was, therefore, held to be justified.

16. An appeal was carried to the Supreme Court by the Regional Provident Fund Commissioner against the judgment of the Learned Single Judge of this Court. After culling out extracts from the judgment of the Learned Single Judge, the Supreme Court held thus in **Regional Provident Fund Commissioner vs. Dharamsi Morarji Chemical Co.Ltd.**[2] :

> "In view of these salient features found to be well established on the record, in our view, it could not be said that Roha factory only because it is owned by the respondent-Company was not a new establishment or could be treated to be a branch or department of Ambarnath factory which by itself was an establishment admittedly covered by the Act as it was an old establishment since 1921."

The Supreme Court noted that the effect of Section 2A is that where an establishment is found to consist of different departments or branches, even if those departments and branches are situated at different places they would be a part and parcel of the parent establishment. However, in that case "the only connecting link" was

2 1998(3) LLN 932

that both the factories were owned by the Appellant. The Supreme Court held that there was no evidence to indicate any interconnection between the two factories in the matter of supervisory, financial or managerial control. The mere fact that both the factories belonged to a common owner was held not to be sufficient to attract the provisions of Section 2A:

> "That by itself cannot be sufficient unless there is clear evidence to show that there was interconnection between these two units and there was common supervisory, financial or managerial control. As there is no such evidence in the present case on the peculiar facts of this case, it is not possible to agree with the learned counsel for the appellant that Roha factory was a part and parcel of Ambarnath factory or it was an adjunct of the main parent establishment functioning at Ambarnath since 1921."

17. A Division Bench of this Court had occasion to consider the impact of the provisions of Section 2A in **Kadamba Suburban Transport Corporation Ltd. vs. Assistant Provident Fund Commissioner.**[3] In that case, the Government of Goa had initially incorporated a company for operating buses on long routes. Consequently the Government took a policy decision to set up another Company for City and suburban routes and the Petitioner came to be incorporated. Some of the buses of the erstwhile

3 1999 II CLR 1264

Company were purchased by the new Company, part of the consideration being treated as the share capital of the erstwhile Company in the petitioner. However, the Boards of Directors of both the Companies were different, the shareholders were different and their spheres of operation were different. Employees of both sets of Companies were maintained independently. On these facts, the Division Bench held that though both the Companies were owned by the Government that would not be sufficient to attract the provisions of Section 2A.

V

18. The facts of the present case would have to be assessed on the basis of the plain intendment and language of Section 2A bearing in mind the interpretation that has been placed in the judgments to which a reference has already been made. The material that has been placed on record would show that both the Appellant and the Second Respondent are independent bodies each with its distinct corporate personality. There is absolutely no material to establish that there was a unity of management, supervision, control or employment. The workforce of the Appellant was not the same as that of the Second Respondent.

Each of the two Companies had its own workforce and an employee of one Company was not transferable to the other. There was no financial inter-connection. The only basis on which the First Respondent came to hold that the Appellant is a part of the establishment of the Second Respondent was the agreement dated 1st May 1984 that was entered into between the parties. By the agreement, the Second Respondent permitted the Appellant to use the registered Trade Mark 'Victor' on a non-exclusive basis in the territories of the States of Maharashtra and Madhya Pradesh in relation to four designs of men's undergarments against the payment of royalty. The agreement between the parties undoubtedly does contemplate that the Second Respondent as a registered holder of the Trade Mark would be entitled to ensure that the products manufactured by the Appellant met the standard of quality that was associated with the mark of the Second Respondent. The conditions that have been imposed in the agreement in that regard are only intended to subserve the object of ensuring that the distinctiveness of the Trade Mark of the Second Respondent is not diluted. A Trade Mark has associated with it the goodwill generated by the business of the owner. A proprietor of a mark who permits the use of the mark by another,

a

is entitled to impose conditions that ensure that the goodwill associated with the mark is not diluted and that the distinctiveness of the mark is not obliterated. The conditions of such an agreement, in this case, however, do not efface the position that both the Appellant and the Second Respondent were independent entities which had entered into an arms length transaction for a limited purpose. The Appellant produced material to indicate that it was engaged in the manufacture of several products besides those for which it was licensed by the Second Respondent. The balance-sheet of the Appellant for the year ending 31st March 1985 showed total sale of Rs. 53.58 lakhs against which royalty payable to the Second Respondent was only Rs.2,39,999/-. The royalty, therefore, constituted 0.55% of the total income from sales. Similarly, the material produced by the Appellant showed that gents undergarments manufactured under licence for that year constituted approximately 2227 dozen valued at Rs. 1.5 lakhs while similar products of the Appellant which were not under licence were to the extent of 4438 dozen valued at Rs. 5.18 lakhs. Apart from this, there is absolutely no evidence of functional integrality. The closure of the unit of the Appellant would not result in the closure of the unit of the Second Respondent or vice versa.

There is no commonality of ownership, management or of the workforce.

19. In these circumstances, the finding of the Learned Single Judge in affirming the order passed by the First Respondent is clearly in error. The decision of the First Respondent was clearly contrary to the law as interpreted in the judgment of the Supreme Court in **Dharamsi Morarji** (supra) and the judgments of this Court to which a reference has been made earlier.

VI

20. In the circumstances, the appeal will have to be allowed and is accordingly allowed. The judgment of the Learned Single Judge dated 19th February 1997 shall stand set aside. The order passed by the First Respondent treating the establishment of the Appellant as a part of the establishment of the Second Respondent is quashed and set aside. However, while disposing of the petition, it is clarified that upon the expiry of the period of protection under Section 16 of the Act, as it then stood at the material time, the Appellant would be liable to be covered by the

provisions of the Act albeit as an independent and separate establishment. Rule in the petition filed by the Appellant under Article 226 of the Constitution shall accordingly stand absolute in terms of the aforesaid directions. However, in the circumstances of the case, there shall be no order as to costs.

(R. M. S.KHANDEPARKAR, J.)

(DR.D. Y. CHANDRACHUD, J.)