

## HR Law Hotline

August 12, 2014

### SUCCESSOR EMPLOYER HELD LIABLE FOR SOCIAL SECURITY DEFAULT PRIOR TO TRANSFER

- Transferor entity had defaulted on its social security obligations towards its employees, prior to the date of transfer.
- As per the agreement between the transferor and the transferee, the transferor entity continued to be liable for payment of any damages to the provident fund authorities for defaulting on its social security obligations.
- Irrespective of an express agreement, transferee entity was held liable to pay damages to the provident fund authorities for default in payment of contributions by the transferor entity, during the period preceding the transfer.

The Supreme Court of India (“**Supreme Court**”) has, in a recent judgment<sup>1</sup>, held the successor employer liable to pay damages for any default in remitting provident fund (social security) contributions. While the default was committed by the transferor entity prior to the date of transfer of employees, the Supreme Court has clarified that the successor employer (i.e. the transferee) shall not stand absolved of the liabilities even if such liabilities have been specifically assigned to the transferor entity by way of an express agreement.

#### BACKGROUND

The appellant in the instant case, McLeod Russel India Limited (formerly known as Eveready Industries (India) Limited) (“**Transferee Company**”) acquired M/s. Mathura Tea Estate, owned by Saroda Tea Company Limited (“**Transferor Company**”). The Transferor Company had defaulted in remitting the contributions and accumulations payable under the Employees’ Provident Fund and Miscellaneous Provisions Act, 1952 (“**EPF Act**”) and the schemes framed thereunder. At the time of acquisition, the proceedings initiated by the Regional Provident Fund Commissioner, Jalpaiguri, West Bengal (“**RPFC**”) to recover dues and impose damages were ongoing. The Transferor Company and the Transferee Company had entered into a memorandum of understanding which specifically attributed any liability with respect to damages payable on account of failure to deposit dues under the EPF Act, to the Transferor Company.

The RPFC held that on a conjoint reading of Sections 14B<sup>2</sup> and 17B<sup>3</sup> of the EPF Act, damages under Section 14B were recoverable jointly and severally from both the Transferor Company and the Transferee Company, with a penalty at an interest rate of 12% per annum, for the delay in depositing damages within the stipulated period, under Section 7Q<sup>4</sup> of the EPF Act.

The decision of RPFC was challenged before a single-judge bench of the Kolkata High Court. The court held that punitive liability of a transferee company could not arise prior to the transfer being implemented. On a further appeal, the division bench of the Kolkata High Court reversed the above dictum laid down by the single-judge bench by placing reliance on the judgment rendered by the special three-judge bench of the Kolkata High Court in *Dalgaon Agro Industries Limited v. Union of India*<sup>5</sup>. The instant case is an appeal against the judgment of the division bench of the Kolkata High Court.

#### ISSUE RAISED

The question before the Supreme Court was whether the Transferee Company would be liable to pay damages for default committed by the Transferor Company in payment of provident fund contributions.

#### JUDGMENT

In addressing the question as to whether the Transferee Company could be held liable under Section 14B of the EPF Act for defaults committed prior to the acquisition, the Supreme Court examined Sections 2(e), 7A, 7Q, 8, 11(2), 14B and 17B of the EPF Act, pertaining to definition of an ‘employer’ and recovery of dues/ damages and interests from an ‘employer’ in cases of default. Section 17B of the statute stipulates that in case of a transfer of establishment, the transferor and the transferee entities shall jointly and severally be liable to pay the contribution and other sums due from the employer under any provision of the EPF Act and the schemes framed thereunder, with respect of the period up to the date of such transfer. The liability of the transferee shall however be limited to the value of the assets obtained by him by such transfer.

The Supreme Court:

- observed that the EPF Act is a beneficial legislation and hence needs to be construed in the best interest of the employees.
- held inter-se covenants between the two entities would not insulate the new employer from the rigours of damages imposed by the EPF Act.
- affirmed the decision of the RPFC, and held that the Transferee Company can be made liable for ‘damages’ as the

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language in Section 17B specifically speaks of “contributions and **other sums due** from the employer”.

## ANALYSIS

This decision of the Supreme Court has provided clarity on successor liability with respect to the EPF Act in case of transfer of an establishment. It signifies the importance of carrying out a thorough due diligence, *inter alia*, on employment related aspects prior to acquisition of one company by another. As a result of this judgment, it becomes more critical for the potential acquirer to assess the dues, damages and liabilities of the seller under the EPF Act and other applicable labour laws and seek appropriate and adequate indemnification in the definitive documentation executed between the parties.

- Vikram Shroff

<sup>1</sup> *McLeod Russel India Limited vs. Regional Provident Fund Commissioner, Jalpaiguri and others*, 2014(8)SCALE272

<sup>2</sup> **Section 14B: Power to recover damages-**

Where an employer makes default in the payment of any contribution to the Fund: the Pension Fund or the Insurance Fund or in the transfer of accumulations required to be transferred by him under sub-section (2) of section 15 or sub-section (5) of section 17 or in the payment of any charges payable under any other provision of this Act or of any Scheme or Insurance Scheme or under any of the conditions specified under section 17, the Central Provident Fund Commissioner or such other officer as may be authorised by the Central Government, by notification in the Official Gazette, in this behalf may recover from the employer (by way of penalty) such damages, not exceeding the amount of arrears, as may be specified in the Scheme:

Provided that before levying and recovering such damages, the employer shall be given a reasonable opportunity of being heard:

Provided further that the Central Board may reduce or waive the damages levied under this section in relation to an establishment which is a sick industrial company and in respect of which a scheme for rehabilitation has been sanctioned by the Board for Industrial and Financial Reconstruction established under section 4 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986), subject to such terms and conditions as may be specified in the Scheme.

<sup>3</sup> **Section 17B: Liability in case of transfer of establishment-**

Where an employer, in relation to an establishment, transfers that establishment in whole or in part, by sale, gift, lease or licence or in any other manner whatsoever, the employer and the person to whom the establishment is so transferred shall jointly and severally be liable to pay the contribution and other sums due from the employer under any provision of this Act or the Scheme or the Pension Scheme or the Insurance Scheme, as the case may be, in respect of the period up to the date of such transfer.

Provided that the liability of the transferee shall be limited to the value of the assets obtained by him by such transfer.

<sup>4</sup> **Section 7Q: Interest payable by the employer-**

The employer shall be liable to pay simple interest at the rate of twelve per cent per annum or at such higher rate as may be specified in the Scheme on any amount due from him under this Act from the date on which the amount has become so due till the date of its actual payment:

Provided that higher rate of interest specified in the Scheme shall not exceed the lending rate of interest charged by any scheduled bank.

<sup>5</sup> (2006) 1 CALLT 32 (HC)

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