IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.1 OF 2003

Indian Express Newspapers (Bombay) Ltd.)
Express Towers, Nariman Point,)
Mumbai – 400 021) ….Appellant

V/s.

The Commissioner of Income Tax,)
Mumbai City I, Mumbai) ….Respondent

Mr. Sukhsagar Sayal a/w. Mr. Amol Joshi, Ms. Tejasvi Ghag, Mr. Shivam Singh i/b. Ms. Poorvi Kamani for appellant.
Mr. P.C. Chhotaray for respondent.

CORAM : K. R. SHRIRAM &
DR. NEELA GOKHALE, JJ.
DATED : 8th MARCH 2024

ORAL JUDGMENT (PER K.R. SHRIRAM, J.) :

1 On 16th September 2004 the following two substantial questions of law were framed :

> *1. Whether the Appellate Tribunal is right in law in holding that the liability for salary and wages arising out of the Justice Palekar Award is not allowable as expenditure in the present year but only in the year in which the agreement between the Management and the employees is entered into?*
>
> *2. Whether the Appellate Tribunal is right in law in holding that exgratia bonus paid to the employees over and above the eligible bonus under the Payment of Bonus Act is not allowable as expenditure under Section 37 (1) of the Act?*

2 Assessee/Appellant is engaged in the business of printing and publishing of News Papers and Periodicals. The matter at hand pertains to Assessment Year 1987-1988. During the assessment year in question, the

Assessing Officer made the following disallowances :

(a) Provision for additional salary and wages amounting to Rs.17 lakhs arising out of the Justice Palekar Award for the period 1st January 1986 to 30th June 1986 on the basis of the Memorandum of Settlement between the management and the employees signed on 8th May 1987;

(b) Exgratia bonus paid amounting to Rs.16,28,258/- over and above the eligible bonus under the Payment of Bonus Act; and

(c) Bad and irrecoverable debts written off Rs.13,65,300/-.

3 Assessee challenged the order before the Commissioner of Income Tax (Appeals) who deleted the disallowances and allowed the amount as deduction in computing assessee's income. The Revenue impugned the order of the CIT(A) before the Income Tax Appellate Tribunal (ITAT) who set aside the findings of the CIT(A) and restored that of the Assessing Officer. It is that order passed by the ITAT on 8th April 2002 which is impugned in this appeal. Only two disallowances matter to this appeal, i.e., additional salary and wages amounting to Rs.17 lakhs arising out of the Justice Palekar Award and exgratia bonus amounting to Rs.16,28,258/- over and above the eligible bonus under the Payment of Bonus Act (the Act).

4 The two questions were answered by the ITAT in a very cryptic manner. As regards question no.1, the Assessing Officer found that there was debit of Rs.17 lakhs representing provision for salary and wages arising out of Justice Palekar Award. The Assessing Officer noticed from the agreement between the management and the employees that memorandum of settlement to reclassification with effect from 1st January 1986 was signed on 8th May 1987, i.e., after the close of the accounting year. The Assessing Officer, therefore, held that the liability to pay additional wages arose only after signing of the agreement. According to the Assessing Officer even under mercantile system of accounting, deduction of the said provision cannot be allowed. It is deductible in the year in which the award was signed and liability was incurred. The Assessing Officer, therefore, disallowed the debit of Rs.17 lakhs. On appeal, the CIT(A) held that the events which have taken place after the close of the accounts can be taken into consideration of the accounts are not finalised and, therefore, providing for the liability in the year of account was justified which is also supported by accounting standard 4.

The ITAT decided the issue in one paragraph by simply stating that the arguments of the learned DR that the impugned liability to pay salary and wages is a contractual liability out of the agreement with the employees and hence, the liability would arise only when it is ascertained

find support from the decision of Allahabad High Court in ***Swadeshi Cotton Mills Co. Ltd. V/s. CIT***[1]. We have to note that the portion, which is quoted allegedly from the judgment, is not found in the copy of the judgment made available to this Court. Be that as it may, this Court in ***Commissioner of Income Tax V/s. United Motors (India) Ltd.***[2] has held on identical facts that the payment by assessee in the aggregate sum to its workmen was for the services that were rendered by them during the previous year under consideration and since such expenditure was incurred for the purpose of earning the income of the previous year, it must be deducted in the previous year. The relevant portion of the judgment reads as under :

> *The gravamen of Dr. Balasubramanian's case is that the liability had not accrued to the assessee in respect of payment to its workmen until after the close of the relevant previous year. This does not appear to us to be, upon the facts, a sustainable proposition. The awards that had governed the terms and conditions of service of the assessee's workmen were terminated. The assessee's board of directors took note of this and made a provision of a sum of Rs.1,00,000 in respect of the impending liability that arose, pursuant to the termination, on account of the revision in the service conditions of its workmen. This was done in the manner of a prudent businessman who knew that the service conditions would have to be bettered. The liability was rightly recognised as having accrued and it was provided for. The provision itself would have been allowable as a deduction. It was not allowed. Instead, the quantified liability in the aggregate sum of Rs.76,680, though it was discharged subsequent to the close of the previous year with which we are concerned, must be allowed as a deduction. The payment in that aggregate sum was made by the assessee to its workmen for the services that were rendered by them during the previous year under consideration. Such expenditure was incurred for the purpose of earning the income of the previous year and must be deducted.*

We respectfully agree with this view.

1 125 ITR 33 (All)
2 1990 (181) ITR 347

5 As regards question no.2, the Assessing Officer found that assessee had paid exgratia bonus amounting in all to Rs.16,28,258/-. The Assessing Officer negatived assessee's claim of deduction in view of first proviso to Section 36(1)(ii) of the Act and observed that the disallowances was subject to rectification and in case it is shown that assessee had allocable surplus to pay bonus of 8.33% he would revise the assessment order. On appeal, the CIT(A) held that the impugned amount is an allowable expenditure under Section 37(1) of the Act. The ITAT, in four lines, set aside the order of the CIT(A) and restored that of the Assessing Officer by simply saying "*On consideration of the arguments advanced by the ld. representatives of the parties, we hold that the findings of the CIT(A) is contrary to the decision of the jurisdictional High Court in CIT vs. Rajaram Bandekar & Sons (Shipping) Pvt. Ltd. 237 ITR 628 (Bom.)*".

Rajaram Bandekar & Sons (Shipping) Pvt. Ltd. (Supra) is of the year 1998. There the Division Bench noted the contention made by assessee that in view of the judgment of this Court in ***Subodhchandra Popatlal V/s. CIT/EPT***[3] it is not open to assessee to contend that the deduction in respect of bonus paid to the employees for the services rendered can be claimed under Section 37(1) of the Act. But in ***Commissioner of Income Tax V/s. Maina Ore Transport P. Ltd.***[4], a Division Bench of this Court, after considering *Rajaram Bandekar & Sons (Shipping) Pvt. Ltd.* (Supra), held

3 (1953) 24 ITR 566
4 (2010) 324 ITR 100 (Bom)

that the Tribunal was justified in holding that the exgratia payment in excess of the limit prescribed under the Payment of Bonus Act, 1965, either under Section 36(1)(ii) or Section 37(1) of the Act was allowable as business expenditure. The Court also held that the Tribunal was justified in holding that exgratia amount paid over and above the amount paid in accordance with the Bonus Act was an allowable expenditure although the payment did not cover contractual payment or customary payment. Paragraphs 7 to 14 of *Maina Ore Transport P. Ltd.* (Supra) read as under :

> 7. *Shri Usgaonkar for the respondent submits that apart from the decision of this court in the case of Raghuvanshi Mills Ltd., there are decisions of other High Courts too taking the same view. The learned counsel placed reliance on the following decisions :*
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> > *CIT v. Shaw Wallace and Co. Ltd. [1991] 190 [TR 455 (Cal), CIT v. Rahimia Lands and Tea Co. P. Ltd. [1992] 197 ITR 310 (Cal) subsequent decision of the Calcutta High Court on the issue. He also relied on the decision of CIT v. Sree Kamakhya Ten Co. P. Ltd. [1993] 199 ITR 714 (Cal), CIT v. National Engineering Industries Ltd. [1994] 208 ITR 1002 (Cal), CIT v. Ganges Rope Co. Ltd. [2001] 252 ITR 524 (Cal) and CIT v. Rajasthan State Mineral Development Corporation [2003] 261 ITR 479 (Raj).*
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> *8. Perusal of the aforesaid decisions of the Calcutta and the Rajasthan High Courts shows that the object of the proviso to section 36(1)(i) of Income-tax Act was to encourage the management to pay bonus in excess of what is statutorily bound to be paid to the employees provided the pay- ment is justifiable as "reasonable payment." It was observed that any other construction of the said provision would be artificial and may not be in, keeping with such a benevolent provision. The decision in the case of Rajasthan State Mineral Development Corporation [2003] 261 ITR 479 (Raj) is somewhat similar to the facts of the instant case. The assessee-company in the said case claimed deduction of exgratia payment to its employees, the Assessing Officer negatived the claim on the ground that the assessee had*

suffered a loss and no outstanding performance has been shown. The appellate authority also confirmed the order of the Assessing Officer. The Rajasthan High Court held that the payment could be allowed under section 37 since it has been incurred wholly or exclusively for the purpose of business. It further held that the payment has been made to maintain industrial harmony and in order to run the business.

9. We may usefully refer to the decision of the apex court in the case of Mumbai Kamgar Sabha v. Abdulbhai Faizullabhai, AIR 1976 SC 1455. (the hon'ble Justice V. R. Krishna lyer and N. L. Untwalia JJ.) The apex court considered the provisions of the Payment of Bonus Act, 1965 particularly, the preamble section 17 which pertains to adjustment of customary or interim bonus and section 34 in respect of effect of laws and claims inconsistent with the said Act. It is observed as below (headnote) :

> *The Bonus Act speaks, and speaks as a whole code, on the sole subject of profit based bonus but is silent on and cannot therefore annihilate by implication, other distinct and different kinds of bonus such as the one oriented on custom. The gravitational pull on judicial construction of Part IV of the Constitution has to some extent influenced this conclusion. Thus it can be held that the Bonus Act (as it stood in 1965) does not bar claims to customary bonus or those based on conditions of services.*
>
> *Schematically speaking, statutory bonus is profit bonus. Nevertheless, there is provision for avoidance of unduly heavy burden under different heads of bonus. For this reason it is provided in section 17 that where an employer has paid any puja bonus or other customary bonus, he will be entitled to deduct the amount of bonus so paid from the amount of bonus payable by him under the Act. Of course, if the customary bonus is thus recognized statutorily and, if in any instance it happens to be much higher than the bonus payable under the Act, there is no provision totally cutting off the customary bonus. The provision for deduction in section 17, on the other hand, indicates the independent existence of customary bonus although, to some extent, its quantum is adjustable towards statutory bonus. Again section 34 only emphasizes the importance of the obligation of the employer, in every case, to pay the statutory bonus. The other sub-sections of section 34 also do not destroy the survival of other types of bonus than provided by the Bonus Act.*

Further it is clear from the long title of the Bonus Act of 1965 that it seeks to provide for bonus to persons employed 'in certain establishments not in all establishments. Moreover, customary bonus does not require calculation of profits, available surplus because it is a payment founded on long usage and justified often by spending on festivals and the Act gives no guidance to fix the quantum of festival bonus; nor does it expressly wish such a usage. The conclusion seems to be fairly clear, unless the court strains judicial sympathy contrarywise, that the Bonus Act dealt with only profit bonus and matters connected therewith and did not govern customary traditional or contractual bonus. The omission to mention the name of a festival as a matter of pleading does not detract from the claim of customary bonus.

10. Learned counsel for the appellant Shri S. R. Rivonkar with his usual to fairness brought to out notice the decision of this court (Division Bench Coram Dr. B. P. Saraf and Dr. Mrs. Pratibha Upasani JJ) in CIT V Rajaram Bandekar and Sons (Shipping) P. Ltd. (1999) 237 ITR 628 (Bom).

11. In the said case reference was made for the opinion of the High Court as regards to the payment of exgratia, to the tune of Rs.1,58,828 to the employees and whether such payment can be deducted as business expenditure by the assessee. This court held that the Tribunal in the said case was not right in holding that the payment of exgratia amount of Rs.1,58,828 to the employees was by way of bonus for the services rendered and accordingly allowable as deduction under section 37 of the Act. The High Court remitted the matter back to the Tribunal for deciding the point afresh thereby giving reasonable opportunity of hearing to the asses see to satisfy the Tribunal that the conditions set out in the second proviso to section 36(1) (ii) are fulfilled. It also directed that the Tribunal if satisfied may allow the deduction under section 36(1) (ii) of the Act.

12. In the instant case, there is no dispute that the amount of Rs.2,37,703 was paid by the assessee to its employees as ex gratia payment. Such payment was over and above the prescribed limits of 8.33 per cent. There is also no dispute that the Commissioner of Income-tax (Appeals), Panaji, as well as the Income-tax Appellate Tribunal have verified that such exgratia payment was made by the assessee. There is also no dispute that the Com- missioner of Income-tax, Panaji and the Income-tax Appellate Tribunal allowed consequential deductions from the assessee's income.

> *13. In the case of Raghuvanshi Mills Ltd. the Division Bench of this court 13 (Coram: Dr. B. P. Saraf and D. R. Dhanuka JJ.) while deciding Income-tax Reference No.169 of 1987 answered the following issues in the affirmative.*
>
> > *1. Whether on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that bonus of Rs.5,26,767 was paid by the assessee-company in excess of 8.33 per cent. was allow- able as a deduction under section 36(1)(ii) and that the restriction imposed by the first proviso to section 36(1) (ii) applied to profit or productions linked bonus and not to other payments?*
> >
> > *2. Whether on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that the additional bonus of Rs.5,26,767 is allowable as a deduction under section 37(1) in spite of specific restrictions imposed by the proviso to section 36(1)(ii)?*
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> *14. For the reasons stated above, we are of the view that the points for reference framed in paragraph 1 above deserve to be answered in the affirmative as the same are covered by the decisions of this court in the case of CIT v. Rajaram Bandekar and Sons (Shipping) P. Ltd. (1999) 237 ITR 628 (Bom) and CIT v. Raghuvanshi Mills Ltd. (Income-tax Reference No. 169 of 1987). Accordingly the reference is answered and the same may be returned to the Tribunal.*

We respectfully agree with this view.

6 In the circumstances, we answer the questions of law in negative. We hold that the ITAT was not right in law in holding that the liability for salary and wages arising out of the Justice Palekar Award is not allowable as expenditure in the present year but only in the year in which the agreement between the management and the employees is entered into. We further hold that the ITAT was not right in law in holding that exgratia bonus paid to the employees over and above the eligible bonus under the Payment of Bonus Act is not allowable as expenditure under Section 37 (1)

of the Act.

7 Appeal disposed accordingly.

(DR. NEELA GOKHALE, J.) (K. R. SHRIRAM, J.)