

(2000) 10 DEL CK 0041

In the Delhi High Court

Case No : Income-tax Reference No. 112 of 1979

Commissioner of Income Tax

APPELLANT

Vs

D.R. Sondhi

RESPONDENT

Date of Decision : 30-10-2000

Acts Referred:

Income Tax Act, 1961 — Section 10(10), 15, 16, 17, 17(3)

Citation : (2001) 1 AD 225 : (2001) 89 DLT 85 : (2000) 57 DRJ 518 : (2001) 248 ITR 695 : (2001) 114 TAXMAN 259

Hon'ble Judges : Dr. Arijit Pasayat, C.J.; D.K. Jain, J

Bench : Division Bench

Advocate : R.C. Pandey and Premlata Bansal, for the Appellant; None, for the Respondent

Judgement

Arijit Pasayat, C.J.—On being moved by the Revenue u/s 256(1) of the Income Tax Act, 1961 (in short "the Act"), the following question have been referred for the opinion of this court by the Income Tax Appellate Tribunal, New Delhi (in short, "the Tribunal") :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal is correct in law in holding that the amount of Rs. 95,000 received by the assessed during this year is to be assessed only u/s 28(ii) of the Income Tax Act, 1961, and that thereby the assessed is entitled to the deduction u/s 80S of the Income Tax Act, 1961 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal is correct in law in holding that where Section 28(ii) applies, Section 15/17(3)(i) of the Income Tax Act, 1961, will not apply even though the assessed is to be described as an employee ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal is correct in law in holding that for the purpose of computing the exemption on account of gratuity u/s 10(10), the word "salary" in that Section would include

the commission earned by the assessed this year ?"

2. The factual position, as indicated in the statement of the case, is as follows :

The assessed is an individual earning income from property, salary and dividends. He was one of the founder-directors of Jullundur Motor Agency Private Limited Company (hereinafter referred to as "a company"). He was originally appointed as a general manager of the company under a resolution of the board dated December 26, 1949. In terms of that resolution, he was allowed a remuneration of Rs. 900 per month, in addition to a commission at 10 per cent, of net profits with effect from January 1, 1960. By resolution dated December 31, 1959, the assessed's designation was changed to "managing director". For the assessment year 1968-69, relating to the previous year ended on March 31, 1968, the following amounts were received by the assessed from the company :

Rs. (a) Compensation 95,000 (a) Gratuity 25,000 (a) Commission 40,000

3. It is to be noted that the company's accounting year relevant to the said assessment year ended on December 31, 1967.

4. For the aforesaid payments two resolutions dated August 27, 1967, and October 23, 1967, are relevant. They are as follows :

"27-8-1967 : Resolved that on his retirement following the sale of the shares in the company, Shri D.R. Sondhi be paid for 1967 up to the date of his retirement commission on profits quantified at Rs. 40,000."

"23-10-1967 : Resolved that a sum of Rs. 95,000 be and is hereby agreed to be paid to Shri D.R. Sondhi, the outgoing managing director, in lieu of his premature retirement and transfer of his shares to which he has agreed leaving no other claim by him regarding the compensation for premature retirement and annuity."

"Resolved further that Shri D.R. Sondhi be paid a sum of Rs. 25,000 for his past services to the company by way of gratuity to which Shri D.R. Sondhi agreed leaving no other claim regarding gratuity on the company."

"Further resolved that the aforesaid two amounts of Rs. 95,000 and Rs. 25,000 by way of compensation for premature retirement, annuity and Rs. 25,000 gratuity being paid to Shri D.R. Sondhi is in view of his special position in the company for his bringing the company to great success and these payments would not be treated as a precedent for the future."

5. The Assessing Officer was of the view that the assessed was an employee of the company. He held that the sum of Rs. 25,000 representing gratuity payment was exempt only up to the limit of the salary specified in Section 10(10) of the Act, and in terms of Section 17 "salary" would include commission, and it would be relevant only for assessment under the head "Salary" and not otherwise. According to him, for the purpose of Section 10(10), "salary" meant only the fixed periodical payment made to a person doing other than manual mechanical work and would not cover payments of commission made/determined with

reference to the profits of the employer. He allowed Rs. 6,750 as exemption out of Rs. 25,000. So far as the sum of Rs. 40,000 received by the assessed is concerned, it was held that the amount would be covered by Section 28(ii) and would qualify for relief u/s 80S. Regarding payment of Rs. 95,000, it was held that the payment was mixed up with the services rendered by the assessed as an employee-director and not for the services rendered in his capacity as a person controlling the majority shares of the company, who managed its affairs through such shareholding. It was held that the payment was nothing but a payment in lieu of salary within the meaning of Section 17(3)(i) of the Act, which also qualified for relief u/s 89 of the Act.

6. The matter was carried in appeal by the assessed before the Appellate Assistant Commissioner (in short "the AAC"). The said authority held as follows :

"(i) Rs. 40,000 could not be treated as capital gain as claimed by the assessed. It was not received by way of transfer of assets. The payment was made in consideration of the assessed's "retirement and past services". The Income Tax Officer was, Therefore, justified in disallowing the assessed's claim that it represented a capital gain.

(ii) Similarly, the amount of Rs. 95,000 received by the assessed could not be treated as capital gain by any stretch of imagination. The Income Tax Officer, however, was not correct in seeking to assess it u/s 17. It was assessable u/s 28(ii) because it represented compensation received by the assessed on the termination of "the managing agency" and the assessed was, Therefore, entitled to relief u/s 80S on this amount.

(iii) The Income Tax Officer was also not correct in limiting the exemption for the gratuity in terms of Section 10(10) to Rs. 6,750 against Rs. 24,000 claimed by the assessed. The assessed's claim was in order because the expression "salary" in Section 10(10) would include the commission also for the purpose of computation of the exemption there under. Hence, the assessed was entitled to a deduction of Rs. 24,000 as against Rs. 6,750 allowed by the Income Tax Officer."

7. The Revenue carried the matter in appeal before the Tribunal challenging the Appellate Assistant Commissioner's conclusions. The Tribunal upheld the conclusions. On being moved, a reference as aforesaid has been made.

8. Learned counsel for the Revenue submitted that the Tribunal lost sight of the true import of Section 17(3)(i) and Section 28(ii) of the Act. Reliance was placed on a decision of this court in *Ishwar Dass Vs. Commissioner of Income Tax*, to buttress the stand. There is no appearance on behalf of the assessed when the matter was called.

9. Section 17(3)(i) and Section 28(ii)(a), which are the pivotal provisions so far as the present case is concerned, read as follows :

"17. "Salary", "perquisite" and "profits in lieu of salary" defined .--For the purposes of Sections 15 and 16 and of this section,-- . . .

(3) "profits in lieu of salary" includes-

(i) the amount of any compensation due to or received by an asses-see from his employer or former employer at or in connection with the termination of his employment or the modification of the terms and conditions relating thereto."

"28. Profits and gains of business or profession.--The following income shall be chargeable to Income Tax under the head "Profits and gains of business or profession",-- . . .

(ii) any compensation or other payment due to or received by,--

(a) any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto ;

(b) any person, by whatever name called, managing the whole of or substantially the whole of the affairs in India of any other company, at or in connection with the termination of his office or the modification of the terms and conditions relating thereto ;

(c) any person, by whatever name called, holding an agency in India for any part of the activities relating to the business of any other person at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto ;

(d) any person, for or in connection with the vesting in the Government, or in any corporation owned or controlled by the Government, under any law for the time being in force, of the management of any property or business ;"

10. The Tribunal found that the materials on record showed that there were two groups involved in the substantial ownerships of the company. The assessed, who was the managing director, went out of the picture along with his group. The resolution dated October 23, 1967, clearly refers to the premature retirement of the assessed and the transfer of his shares while referring to the payment of Rs. 95,000. A finding was recorded by the Tribunal with reference to page 22 of the assessed's paper book, that the assessed and his group sold their shareholding (majority interest) in the company at the time of the assessed's retirement. Section 28(ii)(a), to which we have referred above, deals with a case where any compensation or other payment due to or received by any person, by whatever name called, was managing the whole or substantially the whole of the affairs of the Indian company, or in connection with the termination of his management or the modification of the terms and conditions relating thereto. Such income shall be chargeable to Income Tax under the head "Profits and gains" of business or profession.

11. As the factual position noticed by the Appellate Assistant Commissioner and the Tribunal goes to show, the assessed and his group sold their shareholding

(majority interest) in the company at the time of the assessed's retirement. The resolution dated October 23, 1967, also referred to the premature retirement of the assessed. The payment was not extricably linked with the services rendered by the assessed as an employee-director of the company, as observed by the Assessing Officer. On the contrary, the Appellate Assistant Commissioner recorded that there was some controversy between the two groups of shareholders and it was decided that in the interest of the company, one group of shareholders should part with the other group in the company. Accordingly, the group headed by the assessed together with the other directors representing that group resigned. As a matter of fact, the decision of this court in the case of *Ishwar Dass Vs. Commissioner of Income Tax*, helps the case of the assessed. In that case, the effect of Section 28(ii)(a) was not considered because such a plea was raised for the first time before this court while the reference was being heard. Nevertheless, this court observed that there was force in the contention raised by the assessed about the applicability of Section 28(ii)(a) of the Act. Not only that the court observed that, if law permits, the assessed may refer this claim u/s 28 before any authority in accordance with law. While in civil actions, the expression "compensation" may have peculiar significance, the expression as used in the Act does not appear to be susceptible of only that meaning and no other. The primary significance of the word "compensation" is "equivalence" and the secondary or more common meaning is "something given or obtained as an equivalent". The large number of ways in which this expression "compensation" has been interpreted has one common factor running through them all, that is, that compensation is regarded as an equivalent or recompense, that which makes good the lack of variation of something else. Flowing from this concept enlargement of the meaning of this expression takes in that which compensates for loss or provision, amends, remunerates or recompenses.

12. Our answer to the first question, Therefore, is in the affirmative, in favor of the assessed and against the Revenue.

13. In view of our answer to the first question, there is no necessity to answer the second question.

14. So far as the third question is concerned, in view of our answer to the first question, the Tribunal shall decide afresh whether in the background of what has been held by us, viz., Section 28(ii)(a), the allowance u/s 10(10) is permissible to the assessed,