

(2001) 11 KL CK 0066

In the High Court Of Kerala

Case No : Income Tax A. No"s. 10, 20, 22 and 31 etc. of 2001

Commissioner of Income Tax

APPELLANT

Vs

Ginarajan

RESPONDENT

Date of Decision : 02-11-2001

Acts Referred:

Income Tax Act, 1961 — Section 10(14), 15, 16, 16(1), 17

Citation : (2002) 1 ILR (Ker) 575

Hon'ble Judges : P.K. Balasubramanyan, J;C.N. Ramachandran Nair, J

Bench : Division Bench

Advocate : P.K. Raveendranatha Menon and George K. George, for the Appellant; C. Kochunny Nair, Dale P. Kurian, S. Arun Raj, C.K. Nair, K.M.V. Pandalai and Jacob Thomas, for the Respondent

Judgement

C.N. Ramachandran Nair, J.—The short question arising in all these income tax cases is the "head of income" under which "incentive bonus" received by the assesseees who are development officers employed by the Life Insurance Corporation of India is assessable under the Income Tax Act and the extent of deduction, if any, allowable in the computation of taxable income. While issuing notice in I.T.A. No. 31 of 2001, this Court framed the following three questions of law.

1. Whether, on the facts and in the circumstances of the case, and also in the light of the decision of the Supreme Court in Karamchhari Union, Agra Vs. Union of India and Others, , the Tribunal is right in law in allowing any deduction separately from incentive bonus?

2. Whether, on the facts and in the circumstances of the case, the Tribunal is right in holding:

(i) 30% of the incentive bonus is to be excluded from the definition of "emoluments u/s 17".

(ii) 30% of the incentive bonus should be excluded from the computation at the

inception itself?

3. Whether, on the facts and in the circumstances of the case (and the incentive bonus being salary) the assessee is entitled to any deduction in excess/different from standard deduction allowable/permissible u/s 16(1) of the Income Tax?

2. The assesseees are admittedly regular employees of the L.I.C. of India and are assessed under the head "salary" in respect of the income earned by them from their employer in the form of salary and perquisites. Having regard to the nature of relationship between the L.I.C. of India and the assesseees, as one of the employer and employee, there is no serious dispute under the head of income under which "incentive bonus" also is a assessable. The definition of "salary" u/s 15 of the Income Tax Act is so wide and is only an inclusive one taking in all receipts from the employer in the form of wages, commission, bonus, profit in lieu of or in addition to salary, etc. It is obvious that the legislature did not attach much importance to the euphemism used to describe the payment. Therefore any payment by the employer to the employee towards consideration for service rendered in the course of employment comes within the description of "salary" which included perquisites as well. Probably this is why the assesseees also have not raised any dispute against the assessment of "incentive bonus" received by them from their employer, namely L.I.C. of India under the head "salary". However, the assesseees have raised a serious dispute with regard to the nature and content of incentive bonus received by them from the L.I.C. of India, which is directly related to the business canvased by them and is a percentage of premium received by L.I.C. of India and which is paid over and above the normal salary and perquisites, to which they are entitled. According to the assesseees, sizable amount is spent by them to earn the incentive bonus, and therefore irrespective of the head of income under which the same is assessable, they are entitled to deduction of the expenditure, or in other words, only the net income is assessable. On the other hand, the assessments have been completed treating the incentive bonus as part of the salary and deduction from salary was limited to standard deduction admissible u/s 16 of the Income Tax Act. A separate deduction claimed from out of incentive bonus by the assesseees was ruled out by the Income Tax Department. When the matter went in second appeal to the Tribunal, the Tribunal elaborately discussed the nature of the scheme under which incentive bonus is paid by the L.I.C. of India and relying on a letter issued by the L.I.C. of India to the Central Board of Direct Taxes estimating the expenditure incurred by the development officers at 30% of the incentive bonus accepted the contention of the assesseees and allowed deduction at 30% of incentive bonus towards expenditure, or in other words, sustained assessments only at 70% of the incentive bonus received by the assesseees. In doing so, the Tribunal heavily relied on the decision of the Gujarat High Court in Commissioner of Income Tax Vs. Kiranbhai H. Shelat and Others, .

3. We have heard a batch of cases filed by the department together, wherein the assesseees are represented by various counsel, led by Sri C.K. Nair, and on the

department's side, senior standing counsel Sri. P.K.R. Menon appeared.

4. As the issue arises in the case of assesseees all over India, we have the advantage of several decisions of various High Courts. We will first refer to a Full Bench decision of the Karnataka High Court in Commissioner of Income Tax Vs. M.D. Patil, . The Full Bench took the view that incentive bonus earned by the development officers of the LIC of India is nothing but salary and no deduction over and above the standard deduction provided u/s 16 of the Income Tax Act is permissible under the Income Tax Act. Accordingly, the claim of expenditure or net income theory put forward by the development officers was turned down by the Karnataka High Court. Similar is the view taken by various High Courts including the Andhra Pradesh High Court in K.A. Choudary Vs. Commissioner of Income Tax and Others, , the Madras High Court in Commissioner of Income Tax Vs. E.A. Rajendran, and in Commissioner of Income Tax Vs. P. Arangasamy and Others, that of the Orissa High Court in the decision in C.I.T. v. Anil Singh 215 ITR 224 ; that of the Bombay High Court in The Commissioner of Income Tax Vs. Shri Gopal Krishna Suri and Others, , and that of the Calcutta High Court in Commissioner of Income Tax Vs. Ramlal Agarwala, . However, the assesseees have heavily relied on the decision of the Gujarat High Court in Commissioner of Income Tax Vs. Kiranbhai H. Shelat and Others, which is relied on by the Tribunal while allowing 30% deduction or otherwise sustaining the assessments at only 70% of the incentive bonus received by the assesseees.

5. The Tribunal in its order analysed the nature of incentive bonus with illustration, which is extracted hereunder for convenience:

ILLUSTRATION

Premium collected Rs. 6,00,000/- Lapsed Rs. 1,00,000/- Net eligible premium Rs. 5,00,000/- 20% of Net Rs. 1,00,000/- Annual Remuneration Rs. 5,000/- x 12 = Rs. 60,000/-

Therefore he is eligible to get incentive bonus because the annual remuneration does not exceed 20% of the net premium. If his annual remuneration is above 20% net premium (Rs. 1 lakh) then he will not get incentive. So it is given more as a remuneration and also to increase that basic remuneration. Hence it is in addition to salary.

If he is eligible the calculation of the amount to be given is

Gross premium Rs. 6,00,000/- Lapsed Rs. 1,00,000/- Net eligible premium Rs. 5,00,000/- Remuneration Rs. 5,000/- x 12 = Rs. 60,000/-

Incentive bonus

Rs. 5,00,000 less 5 x 60,000=30,0000=200000 x 6% = 12000

Rs. 5,00,000 less 7 x 60,000=42,0000=80000 x 4% = 3200

Rs. 5,00,000 less 9 x 60,000=54,0000=2% Nil

Total Rs. 15,200/-

From the above, it is clear that the incentive bonus is a percentage of the premium received by the L.I.C. of India for the business canvassed through the development officers. It is not the reimbursement of any expenditure and is not even linked to expenditure, if any, incurred by the development officers. Further, under the Scheme, in cases where the remuneration otherwise received by the development officers is in excess of 20% of the net premium, then the development officer is not entitled to any incentive bonus. There is no explanation from the assesseees as to how the expenditure incurred by them even in such cases can be allowed when no incentive bonus is received, even though business is canvassed, which according to them, involves expenditure. Though the assesseees have vehemently contended that they have sizable expenditure to earn the incentive bonus and the employer, namely, the L.I.C. of India has certified such expenditure having been incurred by them and has even estimated such expenditure at 30%, we have not seen a single case where any assessee has come forward before the department claiming any item of expenditure or furnished details of any such expenditure if at all incurred by him. Therefore, apart from the tall claim made by them, and the help rendered to them by the L.I.C. of India, by writing a letter, there is nothing on record to show that expenditure, if any, has been incurred by any of the assesseees in the course of earning the incentive bonus. Anyhow, we are not influenced by the want of particulars of expenditure, if at all incurred by the assesseees, because such details are required only if any such expenditure is allowable.

6. The question whether any expenditure is allowable in the computation of income or any receipt has to be added to income only after providing for the expenditure is a matter to be found in the statute, that is the Income Tax Act. The scheme of the Act is compartmentalisation of income under various heads and computation of the taxable portion strictly in accordance with the formula of deductions, rebates, and allowances, provided therein. The first step in this regard is to identify the head under which the income is assessable. Deductions and allowances are specific for each head of income. We have already noticed that the assesseees are regular employees of the L.I.C. of India and in view of that the incentive bonus received by them from the L.I.C. of India is assessable only under the head "salary". Sri. C.K. Nair, leading the arguments on behalf of the assesseees, has pointed out that the incentive bonus if at all assessable as salary has to be treated as profit in lieu of salary or in addition to salary as contemplated u/s 17(1)(iv) of the Income Tax Act. He further contended that "profit" in the normal connotation is the net saving after providing for expenditure. According to him, only the net amount that is the incentive bonus after deducting the expenditure has to be taken as income from salary. He heavily relied on the decision of the Gujarat High Court referred to above, which has approved the adoption of the net income after providing for expenses. The assesseees contend that in the absence of proper accounts estimation of expenditure is the only alternative and in view of the certificate issued by the

L.I.C. of India, the expenditure claimed at 30% of the incentive bonus is an acceptable. The department's counsel on the other hand argued that so long as the incentive bonus comes under the head of "salary", the statute does not authorise a deduction towards expenditure claimed by the assessee, whether they have incurred it or not. According to him, such expenditure is only an application of income, and there is no provision for deduction of the same except the standard deduction provided u/s 16(i) of the Act.

7. The assessee has invited our attention to the letter written by the L.I.C. of India to the Central Board of Direct Taxes. We find the details in the decision of the Gujarat High Court referred to above, and also in the impugned order of the Tribunal. The L.I.C. of India has addressed a letter to the Central Board of Direct Taxes in the following lines:

As regards incentive bonus, we have taken note of your clarification in the matter. We are at present designing a new Incentive Bonus Scheme for our Development Officers where it might be possible to provide for a separate allowance or for a distinct/separate element of payment in the nature of reimbursement of expenses which, we know, are necessarily to be incurred in the process of earning that incentive bonus. As this would take some more time, we would request you to allow some relief, in the meanwhile, to our Development Officers on this account.

As you know, incentive bonus is a production-oriented income, inasmuch as higher bonus becomes payable to a Development Officer on achieving higher production. When his actual performance is beyond the normal levels of performance expected of him, he has to incur expenditure in respect of items such as (i) entertainment to agents/clients; (ii) prizes declared in competition among his agents; (iii) conveyance facilities to his agents; and, (iv) office expenses such as rent, secretarial assistance, printing and stationery, postage, trunk calls and telephone charges, etc. The quantum of incentive bonus is decided taking into account factors such as the number of policies procured by a Development Officer, his agency organisation, the nature of territory operated by him, i.e., whether rural or urban, etc. These very same factors also influence the size of his expenditure.

We do not at present allow reimbursement or special allowance as such towards these items, it being understood that a Development Officer is required to spend a part of the incentive bonus on this account. It is therefore, proposed to certify, u/s 10(14) an amount upto 30% of the incentive bonus earned as necessary expenses that would have to be incurred and the internal system devised by us lays down guidelines to the operating offices regarding the percentage to be certified in each case having regard to factors referred to earlier.

We would be grateful if you could kindly examine the points clarified in this letter and issue suitable guidelines to your officers to accept the certification given by the L.I.C. offices both with reference to additional conveyance allowance and

incentive bonus, as above.

The Central Board of Direct Taxes did not accept the request of the LIC of India and sent their reply in the following lines:

3. However such portion of the incentive bonus which is actually spent by the development officer for duties of office can still be exempted from tax if the L.I.C. makes the payment against the expenses incurred by the Development Officers by way of reimbursement of expenses in that case, such reimbursement will not form a part of the "salary" of the Development Officers and only the incentive bonus will appear in their salary certificates.

L.I.C. has not certified that a part of the incentive bonus is against the expenses incurred by the Development Officers by way of reimbursement of expenses. If such a part is certified and that part will not form part of the salary and that part of the incentive bonus which is not certified will appear in the salary certificate. Hence no deduction is contemplated from the incentive bonus, which finds a place in the salary certificates. The finding of the Gujarat High Court page 655 that "however, the facts proved clearly indicate that a part thereof was granted to the employees with a view to meet the expenses that might have to be incurred by him as Development Officer for the discharge of his duty" is, far from being inconsistent with the contents of the letter of the Board, also against law and facts.

Therefore it is obvious that the L.I.C. of India could not convince the Central Board of Direct Taxes that any part of incentive bonus is a reimbursement of expenses. We are told that the L.I.C. of India has now changed their pattern of payment of incentive bonus which is now split into two parts, 70% representing income and 30% towards reimbursement of the expenditure. Since the cases before us do not pertain to any assessment after the introduction of the separate payment by the L.I.C. of India, we are not going into the eligibility of the claim for deduction of 30% now separately given by the LIC of India.

8. We are unable to accept the finding of the Tribunal that 30% of the incentive bonus represents the expenditure at the hands of the assesseees. The Tribunal has stated that assesseees should have expended 30% on account of their activities which are in the nature of training agents, maintaining establishment for the same, etc. We do not find any material to support this finding of the Tribunal. The Tribunal has not gone into the nature of duties of the development officers, for which they are paid usual salary. We requested counsel for the assesseees to clarify the nature of duties of the development officers and from the nature of duties explained by him, we feel what was stated by the Tribunal was part of the normal duties of the development officers for which they are paid salary. It is not out of place to refer to the details furnished in the decision of the Karnataka High Court, wherein the High Court has referred to Schedule III of the Regulation which provides for payment of travelling allowances and reimbursement of other expenses incurred by the development officers in the

normal discharge of their duties. Therefore we find that the incentive bonus which is a share of premium on extra business canvassed is an additional payment whether it can be called as "commission", as was done by the Bombay High Court, or profit in lieu of salary or in addition to salary, as claimed by the assesseees and is nothing but salary coming within the meaning of the term contained in Section 15 of the Income Tax Act. We do not find any provision in the Income Tax Act, except Section 10(14), for allowing deduction towards expenditure of this nature claimed by the assesseees. There is no material to hold that incentive bonus or any part of it is in the nature of reimbursement of expenditure by the employer to the assesseees to qualify for deduction u/s 10(14) can be allowed only if it is granted specifically to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties to the extent such expenses are actually incurred for that purpose. Therefore Section 10(14) does not also apply to the cases at hand for relevant assessment years.

9. Therefore following the decisions of the High Courts referred to above particularly that of the Full Bench decision of the Karnataka High Court in Commissioner of Income Tax Vs. M.D. Patil, and disagreeing with the view of the Gujarat High Court, we are of the view that incentive bonus is only a part of the salary of the assesseees and assesseees are not entitled to any deduction over and above the standard deduction. We are unable to accept the logic adopted by the Gujarat High Court in dissenting the word "profit" occurring in the definition of "salary" and allowing the estimated expenditure portion based on opinion given by the L.I.C. of India without any statutory provision authorising it, in their decision referred to above. The proposition canvassed by the assesseees that incentive bonus is "profit" and the profit in the hands of employees has to be computed after deducting expenditure is against the principle laid down in the decision of the Supreme Court in Karamchari's case, reported in Karamchari Union, Agra Vs. Union of India and Others, . Accordingly in the appeals we answer the three substantial questions of law set out in paragraph 1 above in the negative, in favour of the revenue and against the assessee, set aside the order of the Income Tax Appellate Tribunal and that of the Commissioner of Income Tax (Appeals) and restore the assessments on this issue.

10. The reference cases are disposed by answering the questions referred in favour of the revenue and against the assesseees.