(1997) 01 MAD CK 0070

In the Madras High Court

Case No : Tax Case No. 152 of 1984

Commissioner of Income Tax APPELLANT

Vs

Loyal Textile Ltd. RESPONDENT

Date of Decision : 28-01-1997

Acts Referred:
Income Tax Act, 1961 — Section 147, 148, 149, 256, 27

Citation : (1997) 142 CTR 161 : (1998) 231 ITR 573

Hon'ble Judges : N.V. Balasubramanian, J;Abdul Hadi, J

Bench : Division Bench

Advocate : V. Subramanian, for the Appellant; R. Meenakshisundaram, for the Respondent

Judgement

Abdul Hadi, J.—In this tax case reference by the Revenue, the two questions referred to us under s. 256(1) of the IT Act, 1961 (hereinafter

referred to as ''the Act''), in relation to asst. yr. 1977-78, are :

1. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that the provision of Rs. 2,00,000 made by the

assessee in the accounts for purposes of making contributions to the approved Gratuity Fund should be allowed under s. 40A(7)(b)(i) of the IT

Act, 1961 despite the fact that there was no incremental liability towards gratuity due for the assessment year under consideration ?

2. Whether, keeping in view of the provision in r. 4(2) of Part C of Schedule IV to the IT Act, 1961 and the rules and conditions of the fund as at

the time approval was accorded by the CIT, the adhoc provision of Rs. 2 lakhs is an admissible deduction ?

2. In so far as the abovesaid second question is concerned, learned Counsel for the Revenue himself represents that the said question does not

arise from the order of the Tribunal. Hence, we return the said question unanswered.

3. In so far as the abovesaid first question is concerned, cl. (a) of s. 40A(7) (which came into force w.e.f. 1st April, 1973, by an amendment

introduced by the Finance Act, 1975) provides thus :

Subject to the provision of cl. (b), no deduction shall be allowed in respect of any provision (whether called as such or by any other name) made

by the assessee for the payment of gratuity to his employees on their retirement or on termination of their employment for any reason"".

Then, the abovesaid cl. (b)(i) thereof runs as follows :

Nothing in cl. (a) shall apply in relation to -

(i) any provision made by the assessee for the purpose of payment of a sum by way of any contribution towards an approved gratuity fund, or for

the purpose of payment of any gratuity, that has become payable during the previous year.

While so, the only question to be decided in the present reference is whether the abovesaid expression ""that has become payable during the

previous year"" qualifies both the parts of the said cl. (b)(i), viz. (A), ""any provision made by the assessee for the purpose of payment of any

contribution towards an approved gratuity fund"", and (B) ""any provision made by the assessee for the purpose of payment of any gratuity"" (as

contended by learned counsel for the Revenue) or, qualifies only the latter part, viz. ""any provision made by the assessee for the purpose of

payment of any gratuity"" (as contended by learned Counsel for the assessee-respondent).

4. It is clear to us from a plain reading of the said s. 40(A)(7)(b)(i) that the said clause qualifies both the abovesaid parts. If really it qualifies only

the abovesaid latter part, any amount of provision (or provision to any extent) made by the assessee for the purpose of contribution towards an

approved gratuity fund, would be deductible, which could not be the intention of the legislature in enacting the said provision.

5. That apart, the use of the comma, after the words ""gratuity fund"" and also the words ""any gratuity"" in the abovesaid clause, also indicates that the

said clause qualifies both the abovesaid parts. In Aswini Kumar Ghosh and Another Vs. Arabinda Bose and Another, it has also been observed thus :

When a statute is carefully punctuated and there is doubt about its meaning, a weight should undoubtedly be given to punctuation"".

Likewise in State of Uttar Pradesh Vs. Boota Singh and Others, while considering s. 27 of the Drugs and Cosmetics Act, 1940, which provides

that whoever'' manufactures for sale, sells, stocks or exhibits for sale or distributes'' a drug without a licence, is liable for punishment, the Supreme

Court has held that only stocking for sale could amount to offence and not mere stocking, in view of the presence of comma after ''manufactures

for sale'' and ''sells'' and absence of any comma after ''Stocks''.

6. In the present case, the respondent-assessee had created an approved gratuity fund w.e.f. 26th June, 1974 and during the previous year ending

with 30th June, 1976 relevant to the asst. yr. 1977-78, the assessee made provision in the accounts towards gratuity to the tune of Rs. 2 lakhs,

which amount was also subsequently paid into the said fund, in four instalments subsequent to the said previous year, that is, on 24th July, 1978,

27th July, 1978, 28th July, 1978 and 28th September, 1978. The ITO noticed that while the amount to be provided as on 30th June, 1975 was

Rs. 27,57,274 the liability as on 30th June, 1976 was Rs. 26,44,572 only and that therefore, there was no incremental liability on account of

gratuity for the abovesaid previous year, viz., the year ending with 30th June, 1976 in relation to the abovesaid assessment year in question. He,

therefore, refused to allow the said sum provided for in the account. The assessee went on appeal to the CIT(A). The latter held that inasmuch as

the assessee had paid the said sum subsequently, the provision accorded in the accounts should be allowed as deduction. The Department,

thereupon, went on appeal to the Tribunal. The Tribunal held that with the enactment of s. 40A(7) of the Act, the concept of incremental liability

and the actuarial valuation for the assessment years commencing from 1976-77 had become irrelevant and that those ideas were relevant only

when the provision, made in accounts without payment of the relevant amount into any fund, were being allowed as deduction. It also observed

that after the abovesaid amendment, if a provision for gratuity, without payment of it in the relevant previous year itself into the fund or without the

provision being an actual outgo, is allowed as a deduction, it is only because of payment of that sum into the fund in subsequent assessment years

and not because of any contractual or statutory liability. While so holding, the Tribunal allowed the abovesaid claim of the assessee on the footing

that the abovesaid sum has been paid into the abovesaid fund subsequently in 1978.

7. Thus, it appears that impliedly the Tribunal has interpreted the abovesaid s. 40A(7)(b)(i) in such a way that the abovesaid expression ""that has

become payable during the previous year"" qualifies only the latter of the abovesaid two parts of s. 40A(7)(b)(i). In our view, in view of the reasons

given herein, the abovesaid reading of the Tribunal, of the abovesaid cl. (b)(i), is not correct and the abovesaid expression ""that has become

payable during the previous year"" qualifies both the abovesaid parts of cl. (b)(i).

8. No doubt in relation to the position just prior to the introduction of the abovesaid s. 40A(7), the view taken by Courts was that a provision

made by the assessee in his accounts in respect of estimated service gratuity payable to employees would be deductible in computing the taxable

income in cases where provision has been made on a scientific basis in the form of actuarial valuation. But, that led to some uncertainty in the

matter. That is why the abovesaid Finance Act, 1975 has inserted a new sub-s. (7) in s. 40A. The Supreme Court has also observed in Shree

Sajjan Mills Ltd. Vs. Commissioner of Income Tax, M.P., Bhopal and Another, while considering the question in relation to the assessment years

prior to the coming into force of the abovesaid amendment, that after the abovesaid insertion, of s. 40A(7), deduction for gratuity payment cannot

be allowed on general principles under any other section of the Act. In this connection, the following significant observation of the Supreme Court

may be noted :

Payment of gratuity ...., is the payment made to the employee by the employer on his retirement or termination of his service for any reason ...

The right to receive the payment accrued to the employees on their retirement or termination of their services and the liability to pay gratuity

became the accrued liability of the assessee, when the employees retired or their services were terminated. Until then the right to receive gratuity is

a contingent right and the liability to pay gratuity continues to be a contingent liability qua the employer ... Since the amount of gratuity payable in any given year would be a variable amount depending upon the number of employees who would be entitled to receive the payment during the

year, the amount being a large one in one year and a small one in another year, the employer often finds it desirable and/or convenient to set apart

for future use, a sum every year to meet the contingent liability as a provision for gratuity or a fund for gratuity. He might create an approved

gratuity fund for the exclusive benefit of his employees under an irrevocable trust and make contributions to such fund every year. Contingent

liabilities do not constitute expenditure and cannot be the subject-matter of deduction even under the mercantile system of accounting. Expenditure

which was deductible for Income Tax purposes is towards a liability actually existing at the time but setting apart money which might become

expenditure on the happening of an event is not expenditure"".

Further, the Supreme Court in the abovesaid decision also points out the intention of the legislature in enacting s. 40A(7) by quoting the Notice on

Clauses of the abovesaid amendment, which, inter alia, runs as follows :

In order to remove uncertainty in the matter, it is proposed to specifically provide in the law that no deduction will be allowed, in the computation

of profits and gains of a business or profession, in respect of any reserve created or provision made for the payment of gratuity to the employees

on retirement or on termination of employment for any reason. This restriction will, however, not apply in relation to a provision made for the

purpose of payment of a sum by way of contribution towards an approved gratuity fund that has become payable during the relevant year, or for

the purpose of meeting actual liability in respect of payment of gratuity to the employees that has arisen during such year.

The above referred to underlined words clearly bring about the intention of the legislature in allowing the deduction in relation to the provision made

for the purpose of payment of a sum by way of contribution towards approved gratuity fund. In other words, in such a case also, unless the

abovesaid contribution has become payable during the relevant year, deduction cannot be granted.

9. No doubt, learned Counsel for the respondent relies on the following passage in Commissioner of Income Tax Vs. Andhra Prabha P. Ltd., :

Sub-s. (7) of s. 40A prohibits the deduction of a provision for gratuity. But the prohibition does not extend to the following cases :

(a) provision for contribution to approved gratuity fund, or

(b) provision for payment of gratuity for which a liability has arisen during the year"".

But, it must be stated first of all that the said observation cannot be taken as a ratio decidendi of the said decision, since on facts, the said decision

related only to the asst. yr. 1969-70, that is, much prior to the above referred to introduction of s. 40A(7). That apart, if the above referred to

observation in Commissioner of Income Tax Vs. Andhra Prabha P. Ltd., is taken to mean that only with reference to the provision for payment of

gratuity and not for provision for contribution to approved gratuity fund, the expression ""that has become payable during the previous year"" would

apply, then, we should state with due respect that the above said observation is not correct in the light of the observations in the abovesaid

Supreme Court decision in Shree Sajjan Mills Ltd. Vs. Commissioner of Income Tax, M.P., Bhopal and Another, .

10. Then, with reference to TRIPLICANE PERMANENT FUND LTD. Vs. COMMISSIONER OF Income Tax AND ANOTHER., , relied on

by learned counsel for the assessee, we must state that the said decision does not specifically deal with s. 40A(7) or the provision spoken to

therein, but is concerned with allowability of payment made by the assessee to the gratuity fund. It no doubt refers to the abovesaid observation in

Commissioner of Income Tax Vs. Andhra Prabha P. Ltd., about which we have already expressed our view.

11. In the present case, since it is found that while the gratuity amount as provided as on 30th June, 1975 was Rs. 27,57,274, the liability as on

30th June, 1976 was Rs. 26,44,572 only, it is not possible to hold that the provision made by the assessee was for the purpose of payment of the

sum that has become payable during the previous year. The assessee has also not claimed that the provision of Rs. 2 lakhs made by the assessee

was towards any sum that has become payable during the previous year. Therefore, it has to be concluded that the requirement pursuant to the

expression ""that has become payable during the previous year"" appearing in cl. (b)(i) of s. 40A(7) has not been satisfied, and so, the said cl. (b)(i)

will not apply in the present case and consequently the abovesaid sum of Rs. 2

lakhs cannot be allowed as deduction. No doubt, it appears that

the abovesaid fall in extent of liability was sought to be explained as due to the retirement or resignation, during the year ended with 30th June,

1976 of some of the members of the staff who were eligible for gratuity, (as indicated in the appellate order of the CIT(A). But, it must be noted,

as pointed out by the ITO, that the assessee should have obtained a certificate from the actuary regarding the liability in respect of employees, who

were still in service on 30th June, 1976, so that a comparison between the two figures could have been made and the exact liability as on 30th

June, 1976 ascertained. The assessee has not obtained and produced such a certificate. Therefore, the disallowance of the abovesaid two lakhs of

rupees by the ITO was correct and the first appellate authority and the Tribunal erred in holding differently.

12. Learned Counsel for the respondent also argues that in case we concur with the abovesaid ITO''s view, we should at least make an

observation and also give a direction to the assessing authority to allow the said sum of Rs. 2 lakhs in the succeeding year when the abovesaid sum

of Rs. 2 lakhs was paid into the fund in four instalments as stated above. But, we are of the view that while giving our advisory opinion under s.

256 of the Act in relation to the present assessment year, viz., 1977-78, we have no jurisdiction to make any observation or give any direction in

relation to any succeeding assessment year. No doubt, we realise that in view of the limitations for rectification under s. 154 of the Act, learned

Counsel appears to have made the above referred to request. But, while exercising the present advisory jurisdiction, we have no jurisdiction to

make any such observation or give any such direction as requested by the said learned Counsel. In support of his contention that we have such

jurisdiction, learned Counsel drew our attention to s. 150 of the Act. But, we must point out that s. 150 will not at all help the learned Counsel for

the assessee, s. 150 will come in, only in the case of income escaping assessment, which is dealt with in s. 147 and the subsequent sections. In that

connection only, sub-s. (1) of s. 150 says thus :

Notwithstanding anything contained in s. 149, the notice under s. 148 may be issued at any time for the purpose of making an assessment or

reassessment or recomputation in consequence of or to give effect to any finding or direction contained in an order passed by any authority in any

proceeding under this Act by way of appeal, reference or revision or by a Court in any proceeding under any other law"".

Further, though in sub-s. (1) of s. 150, the above referred to term ""at any time"" is used, sub-s. (2) of s. 150 says thus :

The provisions of sub-s. (1) shall not apply in any case where any such assessment, reassessment or recomputation as is referred to in that sub-

section relates to an assessment year in respect of which an assessment, reassessment or recomputation could not have been made at the time the

order which was the subject-matter of the appeal, reference or revision, as the case may be, was made by reason of any other provision limiting

the time within which any action for assessment, reassessment or recomputation may be taken"".

So, it is clear even in the case of income escaping assessment, no authority can give a direction to make an assessment or reassessment, which

would have been time barred if it had been made at the time when the relevant order was made.

13. Further, s. 150 r/w s. 147 would come into operation only if ""any income chargeable to tax has escaped assessment"". Obviously the present

case is not one such case, where, only the above referred to deduction of provision of abovesaid Rs. 2 lakhs is claimed. While the said deduction

is not allowable for the assessment year in question, in case it is allowable under s. 36(1)(iv) of the Act in the subsequent year in which the above

referred to sum of Rs. 2 lakhs was paid in four instalments, the assessee could only work out his rights, if any, within the four corners of the Act.

Unless such right is still exercisable under any of the provisions of the Act, the assessee cannot get such a right by seeking to get an observation or

finding or direction from us in the way in which it is sought for. As already pointed out, we have no jurisdiction to give any such finding or direction.

14. Learned Counsel no doubt sought to rely on Commissioner of Income Tax Vs. Moduri Rajaiah Gari Kishtaiah, , Commissioner of Income Tax

(Central), Madras Vs. Indian Express (Madurai) Pvt. Ltd., and ABAD FISHERIES Vs. COMMISSIONER OF Income Tax. (AND VICE

VERSA)., : TC 17PS.14. But, in our view they have no application to the issue on hand.

15. The net result is, we answer the abovesaid first question in the negative and in favour of the Revenue and we return the abovesaid second

question unanswered as stated in para. 2 above. No costs.