(2001) 11 KL CK 0068

In the High Court Of Kerala

Case No : Income Tax A. No. 31 of 2001 and connected appeals and ITR No''s. 85, 86 and 255 of 1997

Commissioner of Income Tax — APPELLANT

Vs

T.K. Ginarajan, Development Officer, LIC of India — RESPONDENT

Date of Decision : 02-11-2001

Acts Referred:
Income Tax Act, 1961 — Section 15, 16

Citation : (2002) 253 ITR 463

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

Bench : Division Bench

Advocate : P.K.R. Menon and George K. George, for the Appellant; C. Kochunny Nair, 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 assessees 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 2001 I.T.A. 31 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 Karamchari 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 per cent, of the incentive bonus is to be excluded from the definition of ''emoluments u/s 17'' ?

(ii) 30 per cent 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(i) of the Income Tax Act, 1961 ?"

The assessees are admittedly regular employees of the LIC 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 LIC of India and the assessees, as one of employer and employee, there is no serious dispute as to the head of income under which "incentive bonus" also is 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, profits 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 services rendered in the course of employment comes within the description of "salary" which includes perquisites as well. Probably this is why the assessees also have not raised any dispute against the assessment of "incentive bonus" received by them from their employer, namely, the LIC of India, under the head "Salary", However, the assessees have raised a serious dispute with regard to the nature and content of incentive bonus received by them from the LIC of India, which is directly related to the business canvassed by mem and is a percentage of the premium received by the LIC of India and which is paid over and above the normal salary and perquisites, to which they are entitled. According to the assessees, a 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 the standard deduction admissible u/s 16 of the Income Tax Act. A separate deduction claimed from out of incentive bonus by the assessees 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 LIC of India and relying on a letter issued by the LIC of India to the Central Board of Direct Taxes estimating the expenditure incurred by the Development Officers at 30 per cent, of the incentive bonus accepted the contention of the assessees and allowed deduction at 30 per cent, of the incentive bonus towards expenditure, or, in other words, sustained assessments only at 70 per cent, of the incentive bonus received by the assessees. 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, .

We have heard a batch of cases filed by the Department together, wherein the assessees 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.

As the issue arises in the case of the assessees 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 the 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 Commissioner of Income Tax Vs. P. Arangasamy and Others, ;that of the Orissa High Court in the decision in CIT v. Anil Singh [1995] 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 assessees 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 all owing 30 per cent, deduction or otherwise sustaining the assessments at only 70 per cent, of the incentive bonus received by the assessees.

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

Illustration

Rs.

Premium collected 6,00,000

Lapsed 1,00,000

Net eligible premium 5,00,000

20% of net 1,00,000

Annual remuneration (Rs. 5,000 x 12) 60,000

Therefore, he is eligible to get incentive bonus because the annual remuneration does not exceed 20 per cent, of the net premium. If his annual remuneration is above 20 per cent, 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 as follows :

Rs.

Gross premium 6,00,000

Lapsed 1,00,000

Net eligible premium 5,00,000

Remuneration (Rs. 5,000 x 12) 60,000

Incentive bonus

Rs.

Rs. 5,00,000 less 5 x 60,000 - 3,00,000 - 2,00,000 x 6% = 12,000

Rs. 5,00,000 less 7 x 60,000 - 4,20,000 - 80,000 x 4% = 3,200

Rs. 5,00,000 less 9 x 60,000 - 5,40,000 - 2% = Nil

Total

15,200

From the above, it is clear that the incentive bonus is a percentage of the premium received by the LIC 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 receivable by the Development Officers is in excess of 20 per cent, of the net premium, then the Development Officer is not entitled to any incentive bonus. There is no explanation from the assessees 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 assessees have vehemently contended that they incur sizable expenditure to earn the incentive bonus and the employer, namely, the LIC of India, has certified such expenditures having been incurred By them and has even estimated such expenditure at 30 per cent, 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 LIC of India, by writing a letter, there is nothing on record to show that the expenditure, if any, has been incurred by any of the asscssees in the course of earning the incentive bonus. Anyhow, we are not influenced by the want or particulars of expenditure, if at all incurred by the assessees, because such details are required only if any such expenditure is allowable.

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 assessees are regular employees of the LIC of India and in view of that the incentive bonus received by them from the LIC of India is assessable only under the head "Salary". Sri C. K. Nair, leading the arguments on behalf of the assessees, 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 assessees contend that in the absence of proper accounts, estimation of expenditure is the only alternative and in view of the certificate issued by the LIC of India, the expenditure claimed at 30 per cent, of the incentive bonus is an acceptable one. 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 assessees, 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.

The assessees have invited our attention to the letter written by the LIC 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 LIC of India has addressed a letter to the Central Board of Direct Taxes in the following lines (see page 643 of 235 ITR) :

"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 amongst 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 up to 30 per cent, 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 offices to accept the certification given by the LIC 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 LIC 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.

LIC 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 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 at page 655 that ''however, the facts proved clearly indicate that a part thereof was granted to the employee with a view to meet the expenses that might have to be incurred by him as Development Officer for the discharge of his duty7 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 LIC 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 LIC of India has now changed their pattern of payment of incentive bonus which is now split into two parts, 70 per cent, representing income and 30 per cent, 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 LIC of India, we are not going into the eligibility of the claim for deduction of 30 per cent, now separately given by the LIC of India.

We are unable to accept the finding of the Tribunal that 30 per cent, of the incentive bonus represents the expenditure at the hands of the assessees. The Tribunal has stated that the assessees should have expended 30 per cent, 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 assessees 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 Regulations 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 "commission", as was done by the Bombay High Court, or profit in lieu of salary or in addition to salary, as claimed by the assessees 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 assessees. 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 assessee to qualify for deduction u/s 10(14). In any case, even such an expenditure 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 the relevant assessment years.

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 assessees and the assessees 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 dissecting the word "profit" occurring in the definition of "salary" and allowing the estimated expenditure portion based on the opinion given by the LIC of India without any statutory provision authorising it, in their decision referred to above. The proposition canvassed by the assessees that incentive bonus is "profit" and the profit in the hands of the employees has to be computed after deducting expenditure is against the principle laid down in the decision of the Supreme Court 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.

The reference cases are disposed of by answering the questions referred in favour of the Revenue and against the assessees.