**(1961) 08 P&H CK 0004**

**In the Punjab And Haryana At Chandigarh**

**Case No :** Income-tax Reference No. 16 of 1958

D.N. Bhalla APPELLANT

Vs

Commissioner of Income Tax RESPONDENT

**Date of Decision :** 01-08-1961

**Acts Referred:**

Income Tax Act, 1961 — Section 66

**Citation :** (1961) 08 P&H CK 0004

**Hon'ble Judges :** Khosla, C.J;Daulat, J

**Bench :** Full Bench

# Judgement

Khosla, C.J.—This is a reference u/s 66 of the Indian Income Tax Act made to this court by the Income Tax Appellate Tribunal. The assessee in the case is D.N. Bhalla and the year of assessment is 1952-53, the accounting year being the year ending March 31, 1952. The assessee in this case was employed as the Registrar of the East Punjab University soon after the partition of the State. His appointment was originally made by Ordinance No. 7 of 1947 which established the East Punjab University. The East Punjab Act No. 7 of 1947 took the place of this Ordinance, and u/s 21 of this Act the assessee was appointed as the first Registrar of the University. Section 21 says nothing whatsoever regarding the terms of the office or the conditions upon which his services could be dispensed with. These, however, were set out in the Regulations of the University, and according to Regulation at page 57 of the Punjab University Calendar for the year 1950-51, the assessee was removable on being given six months notice. The wording of the Regulation is as follows :

The Senate may appoint a person to be the Registrar either substantively or as a temporary arrangement. In the case of a substantive appointment, the terms of office shall, in the first instance, be for a period of four years, unless the Senate shall otherwise direct, and the Senate may at any time, on giving six months notice in writing, determine the appointment.

2. Some time in 1949, the assessees services were lent by the East Punjab

 

University to the Government of India. Soon afterwards a notice terminating the assessees services were sent to him. This notice was sent on October 13, 1950, and purported to terminate the assessees services at the end of the period of six months. The notice was served upon the assessee on October 27, 1950. Objection was taken by the assessee to this notice. The nature of his objections is not before us and the objections are not part of the statement of the case, but it is sufficient to note that some objection was taken either to the validity of the notice or to the very notice itself. The matter came up before the Syndicate of the Punjab University on June 16, 1951, and the Syndicate recommended that a mutual agreement be arrived at between the assessee and the East Punjab University. the recommendation of the syndicate was placed before the Senate on July 29, 1951, and the Senate passed the following resolution :

The recommendation of the Syndicate terminating by mutual agreement the services of Shri D.N. Bhalla as Registrar of University with effect from the forenoon of July 18, 1951, on the following conditions, be approved :

(i) that Prof. D.N. Bhalla be paid six monthssalary in lieu of notice and two months additional salary in lieu of privilege leave earned by him;

(ii) that he be paid usual contribution towards the provident fund for eight months referred to on in (i) above;

(iii) that he be permitted to take up any other work during this period."

A copy of this resolution was sent to the assessee and he was asked to send his bill for the amounts due under this resolution. A payment of Rs. 7,200 was, in due course, made to the assessee on account of six months salary under clause (i) of the resolution, and the reference made to us is in respect of this sum of Rs. 7,200. This amount was not included as part of the assessable revenue of the assessee during the accounting year and the decision of the Income Tax department was against him. The following question was thereupon referred to this court upon the assessees application :

"Whether on the facts and circumstances of the case the sum of Rs. 7,200 received from the Punjab University has correctly been treated as a receipt in the nature of a revenue receipt ?

3. The relevant provision of law applicable to the case is contained in Explanation 2 to section 7(1) of the Indian Income Tax Act, 1922, as amended up to 1951. This Explanation is in the following terms :

Explanation 2. A payment due to or received by an assessee from an employer or former employer or from a provident or other fund is to the extent to which it odes not consist of contributions by the assessee or interest on such contributions a profit received in lieu of salary for the purpose of this sub-section, unless the payment is made solely as compensation for loss of employment and not by way of remuneration for past services.

 

4. Therefore, the matter for our consideration is whether the sum of Rs. 7,200 is to be treated as a profit received in lieu of salary or remuneration for past services or on the other hand it is to be treated "solely as compensation for loss of employment." In the latter case, the amount is not assessable to Income Tax, whereas in the former case it is.

5. We have been led through the facts of the case, and it has been argued on behalf of the assessee that the circumstances reveal quite clearly that the amount was paid solely by way of compensation and not in lieu of salary. The third alternative of the amount being in lieu of past services does not arise, because the payment clearly does not fall in that category.

6. Our attention has been drawn to the fact that a notice was served upon the assessee in October, 1950, informing him that his services would be terminated on the expiry of six months. This notice was apparently in accordance with the terms of service as contained in regulation which has been quoted above. Objection was taken to this by the assessee had before us it has been urged that the assessee had a good case because he could have argued that u/s 21 of the East Punjab Act No. 7 of 1947 he could not be removed from service at all, or he could have argued that there was some other defect in the notice. The nature of the objection raised by him is not relevant, and the only matter which is relevant for the purposes of this enquiry is that some objection, which the assessee considered perfectly valid, was raised by him and it was entertained by the Punjab University. Had the objection not been entertained, the notice served upon him in the original instance would have been treated as a valid notice, but the University, in order to terminate the dispute, decided to come to a mutual agreement, and the services of the assessee were terminated in accordance with the terms of this mutual agreement. One of the terms was that the assessee would be paid six months salary in lieu of notice. There were some other terms and some other payments were to be made, but these are not relevant for out purposes. Therefore, it is argued that the six months salary paid to the assessee meant that it was compensation for some rights which the assessee was surrendering or for some privileges of which he was being deprived. It was not payment made in lieu of his rights strictly in accordance with the terms of his employment. In the latter case, he undoubtedly, could not call the payment a compensation, but where he had agreed to give up some of his rights and privileges and receive payment in lieu of them, that payment must be called compensation. On the other hand, it has been argued before us that the terms of employment were set out in Regulation I which required a notice of six months if the Punjab University wanted to terminate the assessees services. In lieu of notice, six months salary could be paid, and this was what was done in the present case. The payment in lieu of notice, therefore, was nothing more than the legal right of the assessee under the terms of employment and it could not be called compensation.

7. I have pointed out that the first notice was not enforced by the Punjab

 

University and the second notice was sent as the result of some negotiations which must have been arrived at between the parties. The result of these negotiations was called a mutual agreement and a recommendation was made by the Syndicate. The recommendation came up before the Senate on the 29th of July, 1951, and the decision arrived at was that in accordance with the terms of the mutual agreement the services of the assessee be terminated with effect from the 18th of July, 1951, i.e., with effect from a date which had already elapsed. This clearly shows that the notice, which was sent as the result of the decision taken by the Senate on the 29th of July, was not a notice of six months which was to take effect from the date upon which it was served as normally would have been the case if the notice had been sent in accordance with Regulation I of the Punjab University. Another circumstances is that if the agreement between the parties was called a mutual agreement, this clearly means that each party was giving up something and both parties were agreeing to abide by a decision whereby the normal legal rights were being left out of consideration. Our attention has also been drawn to a letter which was sent to the assessee at his request in 1953. This was a letter sent to him by the Registrar of the Punjab University and the payment made to him was called a payment in the nature of compensation. I do not think a great deal of importance need be attached to this letter, although it can be argued that as far as the University was concerned, it looked upon the payment as compensation and, therefore, it must have been so and it must have been arrived at as the result of a mutual agreement.

8. Our attention has been drawn to a case of a somewhat similar nature reported as Guff v. Commissioner of Income Tax. In this case an employee of a company was served with a notice in accordance with the terms of his employment. He continued to serve the company for a little more than seven months and then he was paid a sum of Rs. 12,000 on account of six months salary and his services were terminated. The question arose whether this was revenue in lieu of salary or compensation in lieu of loss of employment. The Bombay High Court took the view that it was compensation in lieu of loss of employment and as such was not assessable to Income Tax. The facts of the case before us are somewhat similar to the facts of that case. In that case the notice which was given in the original instance did specifically state that the employees services would be terminated on the expiry of a period of six months for the terms of his employment provided that he was entitled to six months notice. But he remained in service for a period of nearly eight months and then he was paid the sum of Rs. 12,000. In the present case also the six months had expired when the mutual agreement between the parties was arrived at. On the other hand, Mr. Hardy, who appeared on behalf of the department, cited before us Dale (H.M. Inspector of Taxes v. de Soissons. In this case the assessee was employed as an assistant in a company for a period of three years on an annual salary of Pounds 3,000. The terms of his appointment provided that his services would be dispensed with at the end of one or two years. If his services were dispensed with at the end of one year, he

 

was to receive a sum of Pounds 10,000 and if at the end of two years a sum of Pounds 6,000. His services were terminated after he had served the company for a period of one year and he was paid a sum of Pounds 10,000 in accordance with the terms of the agreement. The question arose whether this was revenue or amount paid by way of compensation for loss of employment. It was held that since the agreement provided that he was to be paid a sum of Pounds 10,000 if his services were terminated at the end of one year, it could not be called "compensation". "Compensation" is something which is paid in lieu of loss of certain rights or privileges. In that case it was held that there was no question of any loss of legal rights, because the terms of the agreement were strictly followed. The principle there laid down was followed by a division bench of the Patna High Court in Talwar v. Commissioner of Income Tax. In that case a sum of Rs. 25,200 was paid in accordance with the terms of the agreement to the assessee. Following the principle laid down in Dale (Inspector of Taxes) v. de Soissons, the Patna High Court held that the amount paid was assessable to Income Tax. The learned judges quoted a passage from the judgment in Henry v. Arthur Foster and Henry v. Joseph Foster, and drew attention to the fact that in cases of this nature the determining factor is that the payment to the assessee., what ever the parties may have chosen to call it, is a payment which the company had contracted to make to him as part of his remuneration. If that be so, then it is quiet clear that it cannot be called compensation for loss of service. In the present case I have pointed out the distinguishing features, viz., (1) the original notice was completely disregarded; (2) the notice served upon the assessee took effect not from the date upon which it was served upon him but from a date which had already elapsed; and (3) the notice clearly made mention of the fact that it was being issued in pursuance of a mutual agreement arrived at between the parties. These circumstances clearly show that the payment was not being made in accordance with the terms of employment set out in Regulation I but in accordance with the term of an agreement whereby the assessee agreed to give up the objections which he had raised to issue of the first notice and the University agreed not to enforce the natural consequence of that notice.

9. In this view of the matter, we must answer the question referred to us by saying that the amount of Rs. 7,200 is not revenue receipt but capital receipt. The assessee will recover costs of these proceedings which we assess at Rs. 200.

Daulat, J.

10. I agree.