
(1971) 07 AHC CK 0013

In the Allahabad High Court

Case No : Income Tax R. No. 242 of 1967 connected with I.T.R. No. 241 of 1967

Symonds Distributors (P.) Ltd. and Wheelers Distributors (P.) Ltd. APPELLANT

Vs

Commissioner of Income Tax RESPONDENT

Date of Decision : 07-07-1971

Acts Referred:

Income Tax Act, 1961 — Section 36

Citation : (1972) 86 ITR 88

Hon'ble Judges : S.N. Dwivedi, J;R.L. Gulati, J

Bench : Division Bench

Advocate : V. Sarup and J. Sarup, for the Appellant; B.L. Gupta and R.R. Misra, for the Respondent

Judgement

R.L. Gulati, J.—This is a reference u/s 256(1) of the Income Tax Act, 1961. The following question of law has been referred for the opinion of this court.

"Whether, on the facts and circumstances of the case and where the assessee had kept its books on mercantile system of accountancy and had made a provision for payment of bonus just before the close of the accounting year in pursuance of a resolution of the board of directors, it could rightly be held that the claim for the deduction on the amount for the provision of bonus cannot be allowed as a deduction on the ground that the assessee's profits were not ascertained or known till the final adjustment of the accounts ?"

2. The assessee is a private limited company engaged in the business of sports goods. The assessment year involved is 1962-63, the accounting year being the calendar year 1961.

3. There is a group of three companies including the assessee-company which is managed by the same management. M/s. A. H. Wheeler & Co. (P.) Ltd. is the parent company, while the other two companies are the subsidiaries of M/s. Wheeler Distributors (P.) Ltd. The connected reference relates to M/s. Wheeler

Distributors Company and an identical question arises in that case also. It appears that the parent company has employed the entire staff. The assessee company has no staff of its own. The staff from the parent company is lent to it, but the salaries of the staff are paid by the assessee-company in respect of the time and work done by the staff. In respect of the assessment year 1962-63 the board of directors of the parent company passed a resolution to the effect that the bonus at the rate of two months' salary be allowed to the staff. It was also resolved that a proportionate amount for the payment of the bonus should be recovered from the assessee-company. The assessee-company in its turn passed a similar resolution. The resolution was passed on December 4, 1961, and reads as under :

"Bonus to staff

It was resolved that having regard to the prospects of the company for the year 1961 the company do declare bonus for the year 1961 at the rate of one-sixth of the total basic pay drawn by the staff during the year, the payment to be made after the final accounts for the year have been drawn up."

4. In pursuance of the aforesaid resolution a sum of Rs. 6,500 was earmarked for the payment of the bonus and appropriate adjustment entry was made in the accounts for the calendar year 1961. The assessee claimed this sum of Rs. 6,500 as a deduction in the computation of its net income assessable for the year 1962-63. The Income Tax Officer disallowed the claim principally on the ground that the staff to whom the bonus was payable did not belong to the assessee-company. The Appellate Assistant Commissioner of Income Tax on appeal reversed the finding of the Income Tax Officer. He was of the opinion that the fact that the staff did not belong to the assessee-company was of no consequence. There was an Appeal by the department to the Income Tax Appellate Tribunal. The Tribunal agreed with the view of the Appellate Assistant Commissioner of Income Tax, but disallowed the assessee's claim on another ground, the ground being that as the provision for the bonus had been made before the close of the accounting year, the profits for that year had not been ascertained at the time when the entry was made in the assessee's account books.

5. Now a payment of bonus is allowed as a deduction u/s 36 of the Income Tax Act, 1961, which corresponds to Section 10(2)(x) of the Income Tax Act, 1922. The relevant provision of Section 36 reads as under:

"36. The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in Section 28.....

(ii) any sum paid to an employee as bonus or commission for services rendered, where such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission :

Provided that the amount of bonus or commission is reasonable with reference to--

- (a) the pay of the employee and the conditions of his service;
- (b) the profits of the business or profession for the previous year in question ; and
- (c) the general practice in similar business or profession;....."

6. The Tribunal has not disputed the existence of conditions (a) and (c) referred to above, but has held that condition (b) did not exist. Condition (b) merely stipulates that the admissibility of any sum paid as bonus shall be judged with reference to the profits of the previous year in question. The profit for the relevant previous year in the instant case was a sum of Rs. 61,794. The Tribunal has not taken the view that the amount of profit was inadequate so as to warrant the payment of the bonus. Its view seems to be that since the profit had not been worked out when the provision for the payment of bonus was made, the claim could not be allowed. We are of opinion that the Tribunal was in error in taking that view. The resolution for making the provision for payment of bonus was passed on December 4, 1961, and the accounts of the previous year were to be closed on December 31, 1965, so that the resolution was passed almost at the end of the year. It cannot be said that the board of directors of the assessee-company were not in a position at that time to have an idea of the profits of the company.

7. "Bonus" is not a share or a fraction of profit. It is an amount which is to be fixed with reference to the profits so that it is not necessary that the exact figure of profits should be known before a provision for payment of bonus is made. It is enough if the circumstances of the case show that the directors had an idea of the quantum of profits before a provision for bonus was made. It is true that the bonus was declared during the currency of the previous year. But, the year had almost come to a close when the deduction for the payment of bonus was made. The Income Tax Appellate Tribunal has referred to the case of Commissioner of Income Tax, Madhya Pradesh, Nagpur and Bhandara Vs. Swadeshi Cotton and Flour Mills Private Ltd., . It is difficult to understand as to how that case is relevant. That was a case where a claim was made by the employees for the payment of bonus, but the company did not accept the claim. The matter was referred for adjudication to the Labour Court. It was in that context that the Supreme Court held that the liability of the company for the payment of bonus arose in the year in which the award was given by the Labour Court and as such the company could claim the deduction only in the assessment year which was relevant to the year in which the award was made. The claim could not be made in any previous assessment year, even though the profits out of which the bonus was payable were in respect of an earlier year. No such question is involved in the instant case. There was no dispute between the company and its employees for the payment of bonus. The payment of bonus was voluntary. It can be

assumed that the staff must have made a claim and the management must have accepted it or that there must have been a subsisting understanding between the company and its employees for the payment of bonus in case the company earned good profits.

8. In the instant case it is apparent that payment of bonus was declared by the board of directors after taking into consideration the profit which the company was expected to earn in the calendar year 1961. That is all that the law requires. There is no authority for the view that unless the actual profits are worked out, a declaration for the payment of bonus cannot be made.

9. Now, the importance of the accounts being kept on the mercantile system is that in such a case a deduction in respect of bonus can be claimed when the company incurs the liability to pay the bonus and makes appropriate entries in the books of accounts. The date of actual payment of bonus is immaterial. Under the cash system a deduction can be allowed only when the payment is made. In the instant case, the assessee-company keeps its accounts on mercantile system. It is not disputed that the assessee had incurred a liability, when it passed the resolution. The company had made appropriate entries in the books of accounts. In the circumstances, the company was clearly entitled to the deduction claimed by it regardless of the fact that the actual profits had not been worked out, when the declaration for bonus was made.

10. We accordingly answer the question in the negative in favour of the assessee and against the department. The Commissioner of Income Tax shall pay the costs of this reference to the assessee which we assess at Rs. 200.

income tax Reference No. 241 of 1967.

11. The facts of this case are similar to the facts of the connected case and the question of law is also identical. In this case the resolution for the payment of bonus was passed by the board of directors on 7th of December, 1961, and the accounting year of the company closes on December 31, 1961.

12. For the reasons stated in the connected reference we answer the question in this case also in the negative in favour of the assessee and against the department. The Commissioner of Income Tax shall pay the costs of this reference to the assesses which we assess at Rs. 200.