
(1965) 07 KL CK 0023
In the High Court Of Kerala
Case No : Income Tax R. 14 of 1964

Teekoy Rubbers (India) Ltd.

APPELLANT

Vs

State of Kerala

RESPONDENT

Date of Decision : 19-07-1965

Acts Referred:

Kerala Agricultural Income Tax Act, 1950 — Section 5(j)

Citation : (1965) KLJ 762

Hon'ble Judges : M.S. Menon, C.J;P. Govindan Nair, J

Bench : Division Bench

Advocate : K.P. Abraham, George Kurien, Thomas Vellappally, K.P. Pathrose, E.M. Jacob, K.K. Paulose and M. Pathrose Mathai, for the Appellant;

Judgement

M.S. Menon, C.J.—This is a reference by the Agricultural income tax Appellate Tribunal, Trivandrum, u/s 60 (1) of the Agricultural income tax Act, 1950. The assessee is the Tcekoey Rubbers (India) Limited, Palai. The assessment year concerned is 1960-61; and the accounting period, the twelve months ended on 31--3--1960. The question referred is:

Whether on the facts and in the circumstances, the following gratuity payments made by the applicant company are allowable:

(a) gratuity of Rs.15,000/- paid to the widow of a Superintendent who died while in service of the applicant,

(b) Gratuity of Rs.500/- paid to a Superintendent on termination of his employment with the applicant company

Mr. Hartly whose widow was paid the Rs.15,000/- was, it is admitted, a superintendent of the assessee's estate for a number of years. He died in harness and his widow was given the sum of Rs.15,000/-, calculated at the rate of half-a -month's salary for every year of Mr. Hartly's service.

2. Section 5 of the Agricultural income tax Act, 1950, provides that the

agricultural income of a person shall be computed after making the deductions mentioned in that section. One of the deductions specified reads as follows:

(j) any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of deriving the agricultural income.

3. The contention on behalf of the assessee is that the payment of Rs. 15,000/- to Mrs. Hartly is an expenditure coming within section 5 (j) of the Act. In *Alherten v British Insulated & Helsby Cables Limited* (10 T. C. 155) Viscount Cave L. C. said:

A sum of money expended, not of necessity and with a view to a direct and immediate benefit to the trade, but voluntarily and on the grounds of commercial expediency and in order indirectly to facilitate the carrying on of the business, may yet be expended wholly and exclusively for the purposes of the trade.

This passage was quoted with approval and applied by the Supreme Court in *Commissioner of income tax v Chandufal Keshavlal & Company* (1960-38 I. T. R. 601).

4. In *Gordon Woodroffe Leather Manufacturing Company v Commissioner of income tax* (1962-44 I. T. R. 551), The Supreme Court formulated the test to be applied as follows:

Was the payment made as a matter of practice which affected the quantum of salary or was there an expectation by the employee of getting a gratuity or was the sum of money expended on the ground of commercial expediency and in order indirectly to facilitate the carrying on of the business?

It is not contended that the payment was made as a matter of practice or that it affected the quantum of the salary that was being paid to Mr. Hartly or that Mr. Hartly had any reason to entertain an expectation that such a payment would be made. The submission on behalf of the assessee is that the payment was made in order to demonstrate the interest that the company takes in its employees and their dependents, and to ensure by such a demonstration the loyalty and devoted service of the current and future employees without whose unstinted co-operation the company could not possibly carry on its business with profit and efficiency.

5. A similar argument was advanced but negated in *Gordon Woodroffe Leather Manufacturing Company v Commissioner of income tax* (1962-44 I. T. R. 551). The Supreme Court summed up the argument as follows:

It was argued on behalf of the appellant that the amount had been paid as a matter of commercial expediency and in the interest of the company as an inducement to oilier employees that if they rendered service in a similar manner with efficiency and honesty they would be similarly rewarded. Decisive test, it was submitted, was whether such payments of gratuity were likely in future also

and was the payment made as an incentive to the employees to give their best to the employer and if it was so then the payment was a matter of commercial prudence. It was also submitted that the company had acted not with any oblique motive and its good faith was not in doubt, and in support of the contention several cases were relied upon

and said :

In our opinion on the findings as given the payment in dispute does not fall within the provisions of section 10 (2) (xv) of the Indian income tax Act, 1922. The amount was paid not in pursuance of any scheme of payment of gratuities nor was it an amount which the recipient expected to be paid for long and faithful service but it was a voluntary payment not with the object of facilitating the carrying on of the business of the appellant-company or as a matter of commercial expediency but in recognition of long and faithful service of Mr. J. H. Philips. There was no practice in the appellant company to pay such amounts and it did not affect the quantum of salary of the recipient

Section 10(2)(xv) of the Indian income tax Act, 1922, corresponds to section 5(j) of the Agricultural Income-tax Act, 1950.

6. In this case also there is nothing on record to show that there was any connection between the purpose of the payment and the future conduct of the business of the assessee. The resolution sanctioning the payment might have given a clue; but that resolution is not before us. To these circumstances all that we can do is to conclude that the payment was an ex gratia payment, a mere gift to Mrs. Hartly on her husband's death in harness after many years of faithful service.

7. The payment of Rs.500/- to Mr. Stevenage does not stand on a different footing. It is admitted that the company has a regular gratuity scheme for its labour and that Mr. Stevenage was not entitled to participate in that scheme. This payment also is nothing more than an ex gratia payment unrelated to any legal obligation.

8. It has to be noted that both the amounts paid are referred to as "gratuity" in the question referred for decision. The position as regards "gratuity" is dealt with as follows by Sampath Iyengar;

Normally, a gratuity is not an expenditure for the purpose of business. It is a voluntary payment made after the employee has ceased his connection with the business and, generally speaking, there can be no business purpose in such a payment. Where, however, it is established that there is a practice of the particular employer to grant a gratuity, which practice is known to the employees, it may be inferred that the employees have joined the service in the expectation of being paid a gratuity. That expectation would act as an inducement to the employee to hold on to the service till retirement and thus would facilitate the carrying on by the employer of his business without any

break or interruption. If, over and above such practice and knowledge there is proof that the employees would have stipulated for a salary higher than the one which they accepted, because of the expectation, the character of the payment as a business payment is all the more stronger." (Law of income tax, Fifth Edition, Volume II, Page 1092).

9. Every ex gratia payment to an employee cannot be supported on grounds of commercial expediency. Something more is required; something which postulates a clear nexus between the payment and the future conduct of the business. It is that nexus that is lacking in this case, and as a result we cannot but answer the question referred in the negative as regards both the sums concerned; that is, against the assessee and in favour of the Department. We do so; but in the circumstances of the case without any order as to costs. A copy of this judgment under the seal of the High Court and the signature of the Registrar will be sent to the Appellate Tribunal as required by sub-section (6) of section 60 of the Agricultural income tax Act, 1950.