

K.E. Hansen Vs. Assistant Commissioner of

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Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Apr-18-1996

Appellant : K.E. Hansen

Respondent : Assistant Commissioner of

Judgement :

1. This is an appeal by the assessee against the order of the Commissioner of Income-tax (Appeals) for assessment year 1987-88. The only dispute in this appeal is that the living allowance received by the assessee is exempt under section 10 (14) of the I. T. Act, 1961.

2. In pursuance of an agreement between M/s. Haldor Topsoe A/s of Denmark and National Fertilizers Ltd., the assessee was deputed by the former for the fertilizer project at Bijapure on 5-7-1985. His appointment for a period of two years up to 4-7-1987 was approved by Government of India as technician under section 10 (6) (vii) of the Income-tax Act. Besides salary in Danish Kroner equivalent of Rs. 3,04,870, paid by the Danish company in Denmark, the assessee was paid by National Fertilizers Ltd. a living allowance of Rs. 260 per day aggregating to Rs. 79,040 during the year under consideration for meeting his living expenses. The assessee claimed the same to be exempt under section 10 (14) of the I. T. Act as the amount was received by him as compensation for additional expenses which he was to incur per force during the performance of his service. Reference was made to the following decisions of the Tribunal :-ITO v. R. T. Lawrence 2. ITO v. J. C. Smith [IT Appeal No. 5378 (Delhi) of 1985] 'C' Bench, Delhi.

3. ITO V. Hemingway Raymond [IT Appeal No. 2969 (Delhi) of 1984] Delhi 'D' Bench.

The Assessing Officer rejected the assessee's contention. According to him, the amount was paid to the assessee for meeting his extra cost of living in India as part of his salary but not in connection with the performance of his duties in India and, therefore, it was assessable as part of his salary.

3. The CIT (Appeals) upheld the action of the Assessing Officer. Before him, the assessee placed reliance on the decision of the Gujarat High Court in the case of CIT v. S. G. Pgnatale [1980] 124 ITR 391, wherein the allowance paid by way of reimbursement was held to be exempt under section 10 (14). The CIT (Appeals) however, noticed that in the said decision the Explanation added to section 10 (14) with retrospective effect from 1-4-1962 was not considered. He further noticed that the said Explanation was considered by the Andhra Pradesh High Court in the case of Zdzizlaw Skakuz V. CIT [1986] 158 ITR 420, and it was held that the nature of the allowance received by the assessee was not for the purpose of meeting the expenses incurred for the performance of his duties but for his stay, food, maintenance etc., and, therefore, cannot be called as a special allowance exempt under section 10 (14) of the I.T. Act.

4. The learned counsel of the assess, Shri K. Sampath, brought to our notice the order of the Tribunal in the assessee's case for Assessment year 1986-87, dated 19-12-1991 in I. T. Appeal No. 5084/Del of 1988, wherein the assessee's claim was accepted by following the aforesaid decision of the Gujarat High Court in the case of S. G. Pgnatale (supra) and the three decisions of the Tribunal referred to by the Assessing Officer in his order.

5. The learned departmental representative, Shri R. K. Haldhar, on the other hand, referred to a later decision of the Tribunal in the case of V. Enrico v. ITO [1995] 55 ITD 121, besides the decision of the Andhra Pradesh High Court referred to by the CIT (Appeals) and submitted that the amount of living allowance was not exempt under section 10 (14). He further contended that the assessee was not holding an office or employment of profit and, therefore, section 10 (14) does not apply.

6. The learned counsel of the assessee in reply submitted that in the case of V. Enrico (supra), the assessee was not a permanent employee of the foreign company whereas the assessee before us is a permanent employee of the Danish company. Referring to the decision of the Andhra Pradesh High Court, he submitted that the allowance was paid by the Polish firm whereas in the case under consideration it was paid by the Indian company, viz., National Fertilizers Ltd. He referred to the decision of the Kerala High Court in the case of CIT v. Harry Dennis Boughman [1995] 211 ITR 991, the Supreme Court in the case of CIT v. Kulu Valley Transport Co. (P.) Ltd. [1970] 77 ITR 518, the Supreme Court in the case of CIT v. Vegetable Products Ltd. [1973] 88 ITR 192, and the Tribunal, Bombay Bench 'B' (Third Member), in the case of Sixth ITO v. Narendra V. Patel [1985] 11 ITD 587.

7. We have heard the parties and considered their rival submissions.

Section 10 (14) as it was in force at the relevant point of time read as under : "10. In computing the total income of a previous year of any person.

Any income falling within any of the following clauses shall not be included - (14) any special allowance or benefit, not being in the nature of an entertainment allowance or other perquisite within the meaning of clause (2) of section 17, specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, to the extent to which such expenses are actually incurred for that purpose.

Explanation : For the removal of doubts, it is hereby declared that any allowance granted to the assessee to meet his personal expenses at the place where he ordinarily resides shall not be regarded, for the purposes of this clause, as a special allowance granted to meet expenses wholly, necessarily and exclusively incurred in the performance of such duties;" The allowance which is exempt under this provision is that which is allowed to meet the expenditure by an assessee incurred wholly and exclusively in the performance of his duties of an office or employment of profit. The exemption under this section is to the extent of expenses actually incurred. The Explanation clarifies that any allowance given to an employee to meet his personal expenditure incurred at the place where he

ordinarily performs his duties or where he ordinarily resides shall not be regarded as a special allowance granted to meet the expenditure in the performance of his duties. When the Tribunal decided the issue in the case of the assessee in the earlier year, the said Explanation was not considered, nor was it considered by the Gujarat High Court in the case of S. G. Pgnatale (supra). The said Explanation was introduced by the Finance Act, 1975, with retrospective effect from 1-4-1962.

8. In the case of Zdzizlaw Skakuz (supra), referred to by the CIT (Appeals), it was held by the Andhra Pradesh High Court that the outstation allowance and the hotel charges were merely allowances granted to the assessee to meet his personal expenses at a place where the duties of his office are ordinarily performed and, therefore, not exempt. This case is on the lines of the provisions of the Explanation added by the Finance Act, 1975, Similarly, the Allahabad High Court, in the case of Addl. CIT v. A. K. Misra, ITO [1979] 117 ITR 342, held that city compensatory allowance is granted to meet the personal expenditure necessitated by the high cost of living in big cities, that allowance is not granted with reference to the nature of duties but exclusively with reference to the place of posting and that such an allowance would not, therefore, fall within the Explanation to section 10 (14) (before amendment) and was not exempt from tax. In the case of CIT v. J. Jenkin Thomas [1975] 101 ITR 511, the Madras High Court observed at page 523 of the report that the words "in the performance" had come in for consideration in Nolder (H. M. Inspector of Taxes) v. Walters [1930] 15 TC 380 (KB), which was a case of an aeroplane pilot who was employed by a limited company and who claimed deduction of expenses on telephone etc. in the assessment of his remuneration to income-tax under Schedule E of the U. K. Act. At page 387, Rowlatt, J. had said as follows : " 'In the performance of the duties' means in doing the work of the office, in doing the things which it is his duty to do while doing the work of the office. A man who holds an office or employment has, equally necessarily, to do other things incidentally, and spend money incidentally because he has the office. He has to get to the place of employment, for one thing but it is not in doing the work of the office, which begins when he arrives, and sets to work to perform his duties." The decision of the Gujarat High Court in the case of J. G. Mankad v. CIT [1965] 55 ITR 448, was also referred to in the said decision of the Madras High Court, wherein at page 454 of the report, it was held : "But in both cases the

expenses must be expenses which are wholly and necessarily incurred in the performance of the duties of the office.... The expenses must also be expenses which the assessee is required by the conditions of his service to incur out of his remuneration.... the expenses of traveling between Ahmedabad and Bhavnager could not be said to be expenses incurred by the assessee wholly and necessarily into the performance of the duties of the office of part-time professor of accountancy held by the assessee, for they were incurred partly before the assessee commenced to perform such duties and partly after he concluded them." After referring to these two decisions, the Madras High Court held that under section 4 (3)(vi) [of the I. I. T. Act, 1922, equivalent to section 10 (14) of the I. T. Act, 1961], the special allowance must relate to expenses incurred or to be incurred in the course of the performance of the duties of the office or during the performance of the duties of the office. For instance, a person after he reaches his office has to go on duty to various parts of a city for which purpose he receives certain allowances. That would come within the scope of section 4 (3)(vi) of the 1992 Act. The subsistence allowance in that case was not related to the duties as such. The meaning of the word "subsistence", according to their Lordships, is so clear that it cannot have anything to do with the duties of an office as such. The circumstance that the assessee would have to incur extra expenditure because of his posting in India has really no effect on the problem under consideration. The claim for exemption could be sustained only if it was proved that the subsistence allowance was received specifically for meeting the expenses wholly and necessarily incurred in the performance of the duties. Their Lordships further held : "The fact that it is called a subsistence allowance and the circumstance that it is related to the provision of residence clearly go to show that it is an amount received by the assessee for his own benefit and not for meeting the expenses incurred in the performance of the duties at all. The duties had ended in the office. The assessee would have to stay and subsist somewhere, whether employed in India or in his own country. Any receipt for meeting such expenses would not come within the ambit of section 4 (3)(vi) of the Act as such expenses are not shown to be incurred in the performance of duties. The assessee has failed to make out a claim under section 4 (3)(vi) of the Act." 9. In the case of A. K. Venkiteswaran v. CIT [1973] 92 ITR 233, the Kerala High Court held (as per head

notes) : "It is not sufficient if the expenditure claimed is wholly met in the performance of the assessee's duties or has necessarily to be so met nor is it sufficient if it is shown that it was met exclusively in the performance of the duties of the assessee. The requirements are cumulative and therefore, it must be shown that the assessee was required to spend the amount out of his remuneration not only wholly but also necessarily and exclusively in the performance of his duties. More important is the requirement that it is not 'for the' performance of his duties that he has to spend it but 'in the' performance of his duties. The term 'in the performance' is much narrower in scope than the term 'for the purpose of the performance'. Many items of expenditure may be incurred by an assessee to enable him to perform his duties properly. These are not expenses incurred in the performance of his duties as these are limited to expenses incurred during the process of the performance of the duties. The expenses must be incurred wholly in the discharge of the duties and exclusively in the discharge of the duties. Only such expenditure as is incurred after the process of performance of duties has commenced is deductible." That was a case of claim under section 16 (v) of the I. T. Act in respect of amount of room rent paid by the assessee, on the ground that the conditions of his service required his stay at that particular place and the court held that "even if the assessee were required to stay at a particular place by his conditions of service, expenses incurred by way of payment of rent for the room in which he was staying could not be said to have been incurred 'in the performance of his duties'. The room rent was not, therefore, deductible under section 16 (v)".

10. A contrary view was expressed by the Bombay High Court in the case of CIT v. D. R. Phatak [1975] 99 ITR 14, wherein, after referring to the decision in Lomax (H. M. Inspector of Taxes) v. Newton [1953] 34 TC 558 (Ch. D.) Nolder (H. M. Inspector of Taxes) 's case (supra) and Elwood (H. M. Inspector of Taxes) v. Utitz [1965] 42 TC 482 (CA), their Lordships of the Bombay High Court held that these decisions clearly show that even expenses incurred by way of personal expenses, and even though the incurring of such expenses does not synchronise with the hours of duty, can be claimed as permissible deduction as provided under section 16 (v) and that this aspect of the matter was overlooked by the Kerala High Court in A. K. Venkiteswaran's case (supra) and it would, therefore, be difficult to follow the reasoning and the ratio of that decision. Their Lordships of the Bombay High

Court held at pp. 23 and 24 of the report as under : "Judged by this standard we have to consider whether the compensatory (city) allowance is specifically granted to meet the expenses wholly, necessarily and exclusively incurred in the performance of duties of an office or employment of profit. The mere fact that they are personal expenses or such expenses are incurred at a time which does not synchronise with the hours of duty is not sufficient to come to the conclusion that it is not a permissible allowance. Apart from this the relevant rules clearly show that the assessee is entitled to claim exemption in respect of compensatory (city) allowance under section 10 (14). The very definition of the expression 'compensatory allowance' shows that it is an allowance granted to meet personal expenses necessitated by special circumstances in which the duty is performed. Thus it cannot be said that there is no nexus with the performance of duty when such allowance is received by the assessee. The general rule as indicated by Fundamental Rule 44 about grant of compensatory allowance is that the amount of compensatory allowance should be so regulated that allowance is not on the whole a source of profit to the recipient.

Thus it is not even disputed that the actual amount received by the Government servant is much less than what he ordinarily spends by reason of his posting at a particular place. Therefore, such expenses are wholly, exclusively and necessarily incurred in the performance of the duties. In coming to this conclusion one should not overlook the provisions of Fundamental Rule 11 which provides that ordinarily the whole time of a Government servant is at the disposal of the Government which pays him. The sole object of compensatory (city) allowance is to compensate the Government servant for the extra expenditure which he will be called upon to bear by reason of his posting at a particular place. The receipt of such an amount, in our opinion, has been rightly held by the Tribunal as a permissible allowance under section 10 (14) of the Act." 11. In the case of V. Enrico (supra) decided by the Delhi Bench of the Tribunal, rent-free accommodation and free meal were found to have been given to the assessee in terms of the contract and were held to be perquisite within the meaning of section 17 (2) of the Act being expenditure incurred by the employer and it was held that the same expenditure would have been incurred by the assessee had it not been incurred by the employer. In those circumstances, it was held that section 10 (14)

has no application.

12. In R. T. Lawrence's (supra) to which one of us (Judicial Member) was a party, it was held in similar circumstances that the assessee was clearly entitled to exemption under section 10 (14) of the I. T. Act.

In that case, the decision of the Bombay High Court in the case of D.R. Phatak (supra) and the amendment brought in by Finance Act, 1975, with retrospective effect from 1-4-1962 were also discussed. It was observed that the Explanation did not lay down any blanket prohibition; it only stated that only that allowance which was granted to an assessee to meet his personal expenses at the place where the duties of his office or employment of profit were ordinarily performed by him or at the place where he ordinarily resided shall not be regarded for the purpose of clause (14) of section 10 as a special allowance granted to meet the expenses wholly, necessarily and exclusively incurred in the performance of such duties. In that case also, the Indian company paid living allowance to the assessees who were expatriate personnel of American Company to cover cost of food, servants, laundry, pocket money etc. The assessees were sent to India only for a specific purpose and specific assignment for a limited period. The Tribunal, therefore, held that their ordinary residence was outside India and their ordinary place of duties was USA. Paragraph 18 of the Tribunal's order, which deals with the issues, reads as under : "18. We further agree with the submission of the learned counsel for the assessees that the present assessees could not be said to have ordinarily resided in India. They were assigned to IFFCO only for a limited period. They were drawing their salary outside India and were also employed by KIL outside the country. The only conclusion, therefore, possible is that their ordinary residence was outside India. Similarly, we also cannot say that their ordinary place of work was in India. They were here only for specific purposes and for assignment for a limited period. Their ordinary place of duties was USA. If we keep these facts in mind, then the irresistible conclusion that can be drawn is that the payments made to them by way of reimbursement of their personal expenses was a special allowance liable to exemption under section 10 (14). Our this finding is also in accordance with the view taken by the Supreme Court of Canada in Percy Walker Thomson v. Minister of National Revenue, a case which was cited before us by the

learned counsel for the assessee. The departmental contention in all these appeals on this point, thus fails." 13. The contention of the learned departmental representative that the assessee was not holding office or employment of profit and, therefore, section 10 (14) does not apply, has no force in view of the decision of the Andhra Pradesh High Court in the case of CIT v. Maddi Sudarsanam [1988] 174 ITR 659, wherein it was held that a director of nine companies held an "office" within the meaning of section 10 (14), that the expression "office or employment of profit" should be read as "office" employment of profit". The words "of profit" qualify "employment" and not "office" and it would be enough if a person was holding an office and for the purpose of performing the duties associated with that office, he is granted an allowance or benefit specifically to meet the expenses. We, therefore, hold that even if the "living allowance" is in the nature of income from "other sources", the provisions of section 10 (14) would be applicable as the assessee was holding an office within the meaning of this section.

14. In view of the conflicting views of various High Courts and there being no decision by the jurisdictional High Court on the issue, we adopt the view favourable to the assessee and hold that the assessee being a personnel of the Danish company who came to India for a limited purpose and for a limited duration of 2 years, India cannot be his ordinary place of residence, nor a place where the duties of his office are ordinarily performed. The 'living allowance' received by the assessee, in our opinion, therefore, would be exempt under section 10 (14) and would not be hit by the provisions of Explanation to section 10 (14).

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