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Commissioner of Income-tax Vs. Gestetner Duplicators Pvt. Ltd.

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Court : Kolkata

Decided On : Feb-08-1977

Reported in : [1977]110ITR46(Cal)

Judge : Sankar Prasad Mitra, C.J. and ;S.C. Deb, J.

Acts : Income Tax Act, 1961 - Section 36(1) - Schedule - Rules 2 and 4; ;Employees' Provident Funds Act, 1952

Appeal No. : Income-tax Reference Nos. 156, 398, 399 and 400 of 1969

Appellant : Commissioner of Income-tax

Respondent : Gestetner Duplicators Pvt. Ltd.

Advocate for Def. : Debi Pal and ;Anil Roy Chowdhury, Advs.

Advocate for Pet/Ap. : Amiya Kumar Bose and ;Ajit Sengupta, Advs.

Judgement :

Deb, J.

1. Common questions of law and facts are involved in these two references under the Income-tax Act, 1961. The question referred to this court in Income-tax Reference No. 156 of 1969 is as follows :

'Whether, on the facts and in the circumstances of the case, the sums of Rs. 95,421, Rs. 1,00,564 and Rs. 1,17,969 disallowed by the Income-tax Officer out of the total contributions made by the assessee towards the provident fund were allowable under Section 36(l)(iv) of the Income-tax Act, 1961, for the assessment years 1962-63, 1963-64 and 1964-65, respectively ?'

2. The question called for by the court in Income-tax References Nos. 398, 399 and 400 of 1969 runs thus :

'Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the provident fund maintained by the assessee satisfied the condition laid down in Rule 4(c) of the Fourth Schedule, Part 'A', of the Income-tax Act, 1961 ?'

3. The assessee is a private limited company. The company is a manufacturer and seller of duplicating machines and accessories. It had different categories of salesmen in its regular employment. Besides paying salary, the company paid commission to its salesmen in terms of the contract with them. The commission varied both as to rates and different classes of sales inter se the different categories of salesmen. The company maintained a regular provident fund which was recognised by the Commissioner of Income-tax in 1937 and such recognition was in force during the relevant years.

4. In the accounting years relevant to the aforesaid assessment years the company contributed, out of its own monies, to the individual accounts of those employees in the said provident fund on the basis of salary and commission paid to those salesmen, and claimed those amounts as allowable deductions under Section 36(1)(iv) of the Income-tax Act, 1961. Out of such total contributions, the Income-tax Officer disallowed the amounts mentioned in question No. 1, for those amounts pertained to commission for the assessment years stated therein by rejecting the company's contention that since the word 'commission' has been included in the term 'salary' as defined in Rule 2 of the company's recognised provident fund scheme, those sums were allowable deductions.

5. Three appeals, for the aforesaid three years, filed by the company were heard by two different Appellate Assistant Commissioners: one of them rejected the appeal for the assessment years 1962-63 in view of the Rule 2(h) of Part A of the Fourth Schedule to the Income-tax Act, 1961, but the other Appellate Assistant Commissioner allowed the appeals for the other two assessment years by accepting the company's contention. The Tribunal allowed the appeal filed by the company and rejected the appeals filed by the department. Hence, the above questions are now before us.

6. Rule 2 of the provident fund scheme of the company provides as follows:

''Salary' or 'wages' mean only the fixed monthly salary and the commission received by each employee from the company, together with such dearness allowance as may be paid by the company, and shall not include any bonus or overtime or other remuneration or profit whatsoever derived by the employees.'

7. The above rule of the company ex facie recognises the distinction between the fixed monthly salary and commission, though it includes commission within the ambit of the term 'salary'. It also shows that the monthly salary is a fixed amount, whereas the amount of commission is neither fixed nor necessarily payable monthly.

8. Now, subject to such limits as may be prescribed for the purpose of recognising the provident fund, contribution made by an assessee-employer towards a recognised provident fund is deductible under Section 36(1)(iv) of the Act. Part A of the Fourth Schedule to the Act deals with recognised provident fund. Rule 2 provides that :

'unless the context otherwise requires--...

(c) 'contribution' means any sum credited by or on behalf of any employee out of his salary, or by an employer out of his own monies, to the individual account of an employee, but does not include any sum credited as interest;...

(h) 'salary' includes dearness allowance, if the terms of employment so provide, but excludes all other allowances and perquisites.'

9. Rule 3(1) of Part A provides that if, in the opinion of the Commissioner of Income-tax, the conditions prescribed in Rule 4 and the rules made by the Board in this behalf are satisfied he may recognise the provident fund and at any time may withdraw such recognition if, in his opinion, the provident fund contravenes any of those conditions. Clauses (b) and (c) of Rule 4 run thus ;

'(b) the contributions of an employee in any year shall be a definite proportion of his salary for that year, and shall be deducted by the employer from the employee's salary in that proportion, at each periodical payment of such salary in that year, and credited to the employee's individual account in the fund;

(e) the contributions of an employer to the individual account of an employee in any year shall not exceed the amount of the contributions of the employee in that year, and shall be credited to the employee's individual account at intervals not exceeding one year.'

10. Contribution of an employee as provided in Rule 2(c) must come out of his own salary. Clause (b) of Rule 4 enjoins the employer to deduct a definite and a proportionate amount out of the employee's salary for crediting it to the employee's individual account in the fund. Since salary is carried by and belongs solely to the employee, the employer must necessarily contribute his proportionate share out of his own monies. The scheme of the Act also shows that the contribution of the employer must not be less than the proportionate amount contributed by or on behalf of the employee out of his salary. Therefore, any amount, other than the proportionate amount pertaining to dearness allowance and the employee's salary, contributed by an employer must necessarily be excluded for the purpose of recognising the provident fund under Rule 4 of Part A of the Fourth Schedule to the Act.

11. It is now to be noted here that Chapter IXA of the Indian Income-tax Act, 1922, deals with recognised provident fund. The Central Board of Revenue had issued an instruction in the form of a circular being Circular No. 6 of 1941 dated 16th January, 1941, which provided that 'unless commissions and bonuses are fixed periodical payments not dependent on a contingency, they are not covered by the term 'salary' as used in Chapter IXA of the said Act.' Therefore, before any

commission can be termed as salary for the purposes of recognition of a provident fund and for contribution as well under this circular, three pre-conditions must be satisfied, viz., (i) the amount of commission must be a fixed amount; (ii) it must be paid periodically ; and (iii) its payment must not depend on a contingency.

12. In the statement of the case in both the references the Tribunal has stated that in terms of the contract between the company and its employees of the aforesaid categories of salesmen, the company besides fixing' and paying basic salary also pays commission to them 'which varies both in matter of rates as well as on the class of sales inter se between different categories of employees under the head ' salesmen''.

13. The commission payable to different categories of salesmen by the company is, therefore, not a fixed amount. The amounts also vary from salesman to salesman. Payment of commission also depends on various factors, e.g., the output of the company, sales, if any, made by salesmen, etc. If there is no sale in a particular month, no commission is payable by the company to its salesmen, whereas the 'basic salary' is a fixed amount and is paid by the company to each salesman irrespective of sales in terms of the contract between the company and its employees. Therefore, commission payable or paid by the company to its different categories of salesmen cannot be a salary under the above circular.

14. That apart, the meaning of the word 'commission', as stated in Shorter Oxford English Dictionary, volume I (3rd edition), page 349, is a 'pro rata remuneration for work done as agent'. The salesmen of the company are in its regular employment. There is no relation as principal and agents between the company and those salesmen who are not its agents but are mere servants.

15. The meaning of the word 'salary', as stated in the said dictionary, volume II, at page 1781, is a 'fixed payment made periodically to a person as compensation for regular work; now used for non-manual or non-mechanical work (as opposed to wages)'. Therefore, the commission in the instant case cannot in any event fall within the definition of the word 'salary' in Rule 2(h) of Part A of the Fourth Schedule to the Income-tax Act, 196-1.

16. The aforesaid Circular No. 6 of 1941 issued by the Board was in force during the relevant assessment years under Section 297(2)(k) of the Income-tax Act, 1961, In view of the aforesaid provisions of the Act and the Circular No. 6 of 1941, including the meaning of the words 'salary' and 'commission', it must be held that the aforesaid sums are not deductible under Section 36(1)(iv) of the Act as rightly held by the Income-tax Officer and that the Tribunal was wrong in holding that provident fund maintained by the company satisfied the condition in Rule 4(c) of Part A of the Fourth Schedule to the Act.

17. It was, however, urged on behalf of the company, by citing the case of Raja Ram Kumar Bhargava v. Commissioner of Income-tax : [1963]47ITR680(All) , that since the company has paid the commission in terms of the contract to its salesmen, it was a deductible expenditure and the contributions made by the company pertaining to commission to the provident fund is an allowable deduction as it satisfies the definition of the word 'salary' in the company's provident fund scheme. The aforesaid decision is, however, not an authority on the recognised provident fund and reliance on it was misplaced on behalf of the company.

18. It was argued that since the company's provident fund was recognised by the Commissioner and such recognition was not withdrawn in the relevant assessment years, it should be held that the proportionate amounts pertaining to commission contributed by the company to the said fund were wrongly disallowed by the Income-tax Officer. But the commission is not a salary and, therefore, this contention must fail.

19. It was also urged that under Rule 2(c) of Part A of the Fourth Schedule, the word 'contribution' means any sum credited by an employee out of his salary and also any amount contributed by an employer out of his own monies to the individual account of the employee and, therefore, the proportionate amounts pertaining to commission contributed by the company towards the said provident fund out of its own monies are allowable deductions. But the meaning of the word 'contribution' must be read and understood in its own context. The word 'salary' has been used in that definition and, therefore, the contribution to be made by the company to the said fund must be a proportionate amount of salary paid to its

employees. Further, this argument is also inconsistent with thescheme of Part A of the Fourth Schedule and, therefore, it must also fail on this ground.

20. It is also the submission of learned counsel for the company that the expression 'unless the context otherwise requires' used in Rule 2 of Part A is solely referable to the facts and circumstances of the case and, therefore, the word 'salary' as defined in Rule 2(h) of Part A is not applicable to the provident fund of the company inasmuch as the said word has been defined in the company's provident fund scheme. But the expression 'unless the context otherwise requires' is solely referable to the provisions of Part A of the Fourth Schedule and is not at all referable to the facts and circumstances of any particular case, not even to the instant case before us and, therefore, the contention must fail.

21. Reliance was also placed on the last paragraph of paragraph 4 of Circular No. 80 dated March 4, 1972, issued by the Board. It says:

'If the terms and conditions of service are such that commission is paid not as a bounty or benefit but is paid as part and parcel of the remuneration for services rendered by the employee, such payment may partake of the nature of salary rather than as a benefit or perquisite. If, however, on the terms and conditions of service either there is no obligation for the employer to pay the commission or it is a matter purely in the discretion of the employer, such payment should be treated as a benefit by way of addition to salary rather than in lieu of salary.'

22. It was argued that since the commission was paid not as bounty or benefit but in terms of the contract, payment of such commission was a salary. This circular, however, was issued under Section 40(c)(iii) of the Income-tax Act, 1961. It does not apply to Section 36(1)(iv) of the Income-tax Act, 1961, Therefore, we reject this argument.

23. According to the learned counsel for the company, three conditions are required to be satisfied before Section 36(1)(iv) can be applied. Those conditions are :

(a) The sums must be paid by an assessee as an employer;

(b) The sums so paid must be by way of contribution towards the recognised provident fund within the meaning of Section 2(38) of the Income-tax Act, 1961,

(c) The sums so paid must not exceed the limits as may be prescribed for the purpose of recognition of the provident fund.

24. It was contended that the conditions (a) and (b) were satisfied. It was also argued that the condition (c) applies only in the year in which the provident fund is recognised for the first time by the Commissioner which is admittedly not the case before us.

25. Since commission and salary are two different concepts and no commission can be included in salary for the purposes of Part A any sum pertaining to commission contributed by the company towards the said provident fund cannot be treated as contribution within the meaning of that expression. We, however, do not express any opinion on the last contention noted in the preceding paragraph.

26. Definition of the word 'salary' in Rule 2(h) of Part A of the Fourth Schedule is an inclusive definition. It does not, however, define the word 'salary' but within its scope includes dearness allowance and excludes all other allowances and perquisites. This definition was introduced for the first time in the Income-tax Act, 1961. Therefore, it was contended that the last paragraph of paragraph 4 of the Circular No. 80 dated March 4, 1972, should govern the instant case.

27. Though the word 'salary' has not been defined in Chapter IXA of the 1922 Act, for the reasons already stated, this circular must be left out of our consideration. That apart, this circular was not in existence in the relevant assessment years and, therefore, it cannot, in any event, govern the case. Further, the ordinary meaning of the word 'salary' is different from the ordinary meaning of the word 'commission'. The salary is a fixed monthly payment; whereas, the commission is not a fixed monthly payment and, therefore, it cannot be included within the scope and ambit of the term 'salary', the meaning of which cannot also be extended by the company by defining it in its provident fund scheme for the purposes of recognition

of its provident fund and deductibility as well.

28. It was contended finally that if the proportionate contribution pertaining to commission is held not to be an allowable deduction, it would result in an anomalous situation, namely, that the company would be bound to make proportionate contribution pertaining to commission towards the individual account of its employee in the provident fund in terms of its provident fund scheme and the taxing officers would be bound to disallow such contributions. Therefore, we were asked to remove this anomaly in favour of the company by interpreting the word 'salary' used in Rule 2(h) of Part A as stated in the company's provident fund scheme.

29. But there are certain expenditures which are not deductible under the Income-tax Acts, and by no means the courts can make them deductible. Further, a provident fund under the Provident Funds Act, 1952, is also a recognised fund tinder Section 2(38) of the Income-tax Act, 1961. In the case of Bridge and Roofs Co. Ltd. v. Union of India : (1962)IILLJ490SC of the report, it has been held by the Supreme Court that the commission is excluded from the definition of the words 'basic wages' under the Provident Funds Act, 1952, because it is not an universal Rule that each and every establishment must pay commission to its employees. Therefore, the amounts pertaining to commission contributed to a provident fund under that Act cannot come within the scope and ambit of the term 'basic salary'.

30. Since a provident fund under the Provident Funds Act, 1952, is a recognised fund, its provisions and the provisions of Part A of the Fourth Schedule to the Income-tax Act, 1961, should be read and construed harmoniously. When so read and construed, it must necessarily lead to an irresistible conclusion that the commission cannot be included within the meaning of the word 'salary' for the purposes aforesaid.

31. As already stated, the company pays basic monthly salary to its employees and also contributes to the said fund on the basis of the said basic monthly salary and, therefore, in view of the aforesaid decision of the Supreme Court and for the reasons already stated, it must be held that the company's proportionate contribution pertaining to commission is not an allowable deduction under Section

36(1)(iv) of the Act and that its fund does not satisfy the conditions of Rule 4(c) of Part A of the Fourth Schedule to the Act.

32. In the premises, we answer both the questions in the negative and in favour of the revenue. There will be no order as to costs.

Sankar Prasad Mitra, C.J.

33. I agree.

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