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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 01st April, 2022
% *Date of Decision: 13th April, 2022*

\+ **ITA 492/2019 & C.M.No.23180/2019**

SRC AVIATION PVT.LTD. ..... Appellant
Through Dr.Rakesh Gupta with Mr.Somil Agarwal and Mr.Anshul Mittal, Advocates.

versus

ASSISSTANT COMMISSIONER OF INCOME TAX & ANR. ..... Respondents
Through Mr.Sanjay Kumar, senior standing counsel for the Revenue.

\+ **ITA 41/2020 & C.M.No.2840/2020**

SRC AVIATION PVT.LTD. ..... Appellant
Through Dr.Rakesh Gupta with Mr.Somil Agarwal and Mr.Anshul Mittal, Advocates.

versus

ADDITIONAL COMMISSIONER OF INCOME TAX & ANR. ..... Respondents
Through Mr.Sanjay Kumar, Senior standing counsel for the Revenue.

CORAM:
HON'BLE MR. JUSTICE MANMOHAN
HON'BLE MR. JUSTICE DINESH KUMAR SHARMA

J U D G M E N T

DINESH KUMAR SHARMA,J :

1. The SRC Aviation Private Limited has filed these two appeals i.e.ITA 492/2019 & ITA 41/2020 under Section 260A of the Income Tax Act (hereinafter referred to as 'the Act') assailing the Income Tax Appellate Tribunal's (ITAT) order in ITA Nos. 492/2019 & ITA 41/2020 pertaining to assessment year 2011-2012 and 2014-2015 respectively.

2. The facts in brief are that the appellant is a private limited company. Sh.Arvind Chadha and Sh.Anoop Chadha are two share-holders and directors holding 50% equity shares each since inception of the company. In the Assessment year 2011-2012, the company has paid bonus of Rs.1 crore each to both the directors namely Sh.Arvind Chadha and Sh.Anoop Chadha. Similarly in the assessment year 2014-2015 the company has paid bonus of Rs.1.5 crore each to both the Directors. Assessing Officer disallowed the same relying upon Section 36 (1)(ii) of the Act.The Assessing Officer was *inter alia* of the view that bonus was paid to avoid payment of dividend distribution tax.

3. The Commissioner of Income Tax (appeal) in the appeal filed by the Assessee vide orders dated 24.03.2014 and 29.11.2016 confirmed the disallowance and took a view that had the impugned bonus not been paid to these two directors, the amount would have been paid to them as dividend.

4. The order of the CIT (A) was challenged before the ITAT. The Tribunal also agreed with the Assessing Officer and CIT (A) and upheld the order of assessing officer and CIT(A). Aggrieved by the order of the ITAT, the appellants have challenged the order before this Court.

5. The notice was issued and Mr. Sanjay Kumar, Senior Standing counsel accepted the noticeon behalf of the Department.

6. Mr. Rakesh Gupta, learned counsel for the appellant submitted that

the appellant company had been paying bonus to the above working directors apart from the directors' remuneration and the same was being allowed as deductible business expenditure and no disallowance was ever made in the previous assessment years. The remuneration including bonus was paid on the basis of Board resolution for the services rendered by the aforesaid two directors.

7. Learned counsel submitted that both the abovesaid directors declared the bonus as part of the 'salary' under Section 15 of the Act in their returns of income and the same were accepted and assessed as such in their assessments. The directors paid the taxes on their respective income at the highest tax rate. Learned counsel submitted that the assessing officer, CIT (A) and ITAT have committed a grave error by disallowing and wrongly relied upon Section 36 (1) (ii) of the Act. It was submitted that there has to be consistency in the view taken by the revenue authority and since the payment of bonus has all along been accepted by the department, there was no reason to reject the same for these two years.

8. Learned counsel relied upon ***CIT v. Career Launcher India Ltd.***, (2013) 358 ITR 0179 (Delhi**)** and ***AMD Metplast Pvt. Ltd. v. DCIT*** (2012) 341 ITR 0563, ***Controls & Switchgears Contractors Ltd v. DCIT*** 365 ITR 312 (Del) and ***CIT vs. M/s Bony Polymers (P) Ltd.*** ITA Nos.69/2011, 536/2011, 611/2011 & 1298/2011 order dated 18.01.2012. Learned counsel submitted that ITAT has wrongly relied upon ***Dalal & Brocha Stock Broking Pvt. Ltd.*** v. **ACIT** (2011) 131 ITD 36 (Mum)(SB***)***.

9. The learned counsel submitted that the SLP filed by the department in the case of ***CIT vs. M/s Bony Polymers (P) Ltd.*** was dismissed by the Supreme Court vide order dated 24.08.2012.

10. Learned counsel for the appellant submitted that the ITAT has committed a gross error by misinterpreting the provision of Section 36 (1) (ii) and has wrongly made distinction between the facts of the case relied upon by the appellants**.**

11. Learned counsel further submitted that by virtue of the order of the ITAT in this case, the company would be liable to pay tax on this amount, whereas the directors have also paid the tax on such bonus amount in the highest slab tax rate. Learned counsel submitted that therefore on the same amount, there is incidence of double taxation,as the company as well as directors have been subjected to make the payment of income tax at the highest rate which is totally illegal.

12. Learned counsel reiterated that in order to haveconsistency in the order of the revenue, the disallowance made by the authorities below and the tribunal for the year 2011-12 and 2014-15 have to be set aside. It was also submitted that the company as well as the directors have paid tax in the highest bracket and therefore there is no question of escaping the income.

13. Sh. Sanjay Kumar, learned counsel for the department submitted that the present appeals are liable to be dismissed as there is no substantial question of law. Sh. Sanjay Kumar further submitted that the proposition of law is very well settled. It was submitted that in the present case there were only two directors and shareholders in the company. The amount paid to them as bonus is in fact a dividend. It was submitted that the bonus paid to Director (s) is only to avoid tax and to reduce profit of the company and to avoid payment of taxes. Learned counsel for the revenue submitted that in fact he relies upon the same judgments as relied upon by the learned counsel for the appellant. It was submitted that since the proposition of law is very

well settled, the appeals are liable to be dismissed.

14. The short question involved in the present appeals are whether the amount paid to the two directors/shareholders in the assessment years 2011-12 and 2014-15 should be allowed as a deduction or should be included in the income of the company.

15. We have considered the submissions.

16. The scope of jurisdiction in Section 260A is very well settled. It is a settled proposition that ITAT is the final arbiter of the facts. High Court can interfere in the order of the ITAT only if there is substantial question of law or there is manifest illegality or it suffers from perversity. The general rule is that High Court should be slow in interfering into the findings of ITAT, unless it suffers from any of the grounds mentioned hereinabove.

17. Section 36 (1) (ii) of the Act provides as under:

> *"Other deductions.*
> *36. (1) The deductions provided for in the following clauses shall be allowedin respect of the matters dealt with therein, in computing the incomereferred 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 dividendifit had not been paid as bonus or commission."*

18. The interpretation of Section 36 (1) (ii) of the Act has come up for discussion before this Court in several cases including ***AMD Metplast Pvt. Ltd v. DCIT*** 341 ITR 563(Del) *and* ***CIT v. Career Launcher India Ltd.***358 ITR179(Del).

19. In ***Loyal Motor Service Company Limited v. Commissioner of Income Tax*** (1946) 14 ITR 647 (Bom.) it was *inter alia* held as under:

> ***"****Now the facts as shown by the reference are that this company was formed by fourteen persons, thirteen of whom were originally owner- drivers of motorvehicles, the fourteenth member contributing in money. The thirteenth not only contributed their motor vehicles but also their services and accordingly become employees of this company. Besides the thirteen there are twenty-eight other employees making a total of forty-one. In the year in question the company granted a bonus at the rate of two months' salary to its forty-one employees and the total sum required to pay this bonus was Rs. 6,084/- of which Rs. 1,954/- went to the twenty-eight other employees and Rs. 4,130/- to the thirteen shareholder employees. It is to be noted that the quantum of bonus paid to each of the shareholder employees was by reference to their salaries and not to their stakes in the company. A tabulated result is set out in the application for this reference and is printed on p. 12 of the record. It is there shown that of the thirteen shareholder employees six employees got less bonus than they would have got as dividends if the sum of Rs. 4,130/- had been distributed by way of additional dividends. Five of them got more bonus than such dividends and in the case of two of them the figure works out the same. That is an accident in the sense that the bonus payment being referential to their wages and the dividends being referential to their shares have no relation to each other. Now the answer to the question referred to us depends on the construction that is to be placed upon para (x) of sub-s. (2) of s.10. It should be noted that the body of this sub-section provides an allowance and the qualifying part of it is by way of exception to that allowance. What is to be allowed is "any sum"paid to an employee as bonus or commission for services rendered and the exception is, where "such sum"would not have been paid to him as profits or dividends if it had not been paid as bonus or commission. In the exception the words "such sum" can, in my*

opinion, only refer to the last and the only antecedent, which is "any sum"paid as commission or bonus. Therefore, unless the commission or bonus would be paid to the assessee as profits or dividends the exception to the allowance does not operate. Mr. Setalvad on behalf of the Commissioner has pointed put with considerable force that strictly construed there can hardly ever be a case which comes within the ambit of the exception. Sir Jamshedji Kangaon behalf of the assessee company suggests two such cases, viz., in the case of what is generally called a one-man company which is not unlawful under the Indian Companies Act, and is also a case in which a company, in declaring a dividend, or a partnership, in declaring division of their profits, say that instead of distributing their profits by way of dividends, or shares of profits, they will distribute the amount to themselves, as salaried employees in their own company or partnership, as bonus. We are construing a taxation statute and the subject is entitled to have such a statue strictly construed in his favour. In my opinion,in placing a strict construction on this subsection, the sum expected under the expression "such sum"must be the same sum as is described by the expression "Any sum paid as bonus or commission", and that an equivalent sum even in the two cases where by accident the bonus and the prospective dividend are the same, is not included in that construction. If that is the construction which is to be placed upon this sub-section, then the answer to the question is, that the whole sum of Rs. 4,130/- paid as bonus to the shareholder employees is allowable as deduction under the provisions of s. 10(2)(x). I answer the question referred to us in the affirmative. The Commissioner must pay the costs of this reference."

Kania, J. in his judgment had elucidated and interpreted Section 10(2)(x) of the Income Tax Act, 1922 and observed:

"In my opinion, that the construction of the clause is not correct. The word "such" must refer to what had been previously mentioned in the same clause in connection with the word "sum". To find that out we must look to the first part of the clause. That refers to "any" sum. Reading the clause in that

way the plain meaning appears to be that when a particular amount was paid by way of bonus to an employee, if the same amount would have been paid to him as a shareholder as dividend or profit, the company cannot be allowed a deduction on the ground of payment of bonus. To put it in other words the clause is intended to prevent an escape from taxation by describing a payment as bonus, when in fact ordinarily it should have reached the shareholder as profit or dividend. The argument would be equally applicable in the case of a partnership as in the case of a limited company. This construction leads to no hardship. It does not allow a wrong payment of bonus to escape taxation. In the first instance the bonus in the hands of the employee is liable to be taxed, unless exempted by a special notification. Moreover, the proviso contains conditions under which if a wrong claim is made, the same can be investigated and disallowed. An illustration will perhaps make the position clear. Five persons in a firm realizing that the profits of the year were Rs. 50,000/- and they had an equal share in the profits of the business decide that instead of receiving Rs. 10,000/- each as the share of profits each of them will be paid Rs. 10,000/- as bonus or commission. In such a case the firm, when sought to be assessed, may contend that Rs. 10,000/- were paid as bonus. The contention will be clearly rejected.But the safeguards do not end there. The firm will have to prove to the satisfaction of the taxing authority that five partners were employees, in the first instance.Secondly, that the bonus was a reasonable amount having regard to the pay the employee and the condition of the service.Thirdly, that the profits of the business for the year in question made it reasonable to pay the amount granted as allowance and lastly the general practice in similar business or trade justified the payment of the amount as bonus. It seemsto me that the plain reading of the clause means that the profits of a business will not be allowed to be dwindled by merely describing the payment as bonus, if the payment is in lieu of dividend or profit. I do not see any reason why any strained construction should be put on the plain meaning of the words of the clause. I therefore, agree with the learned Chief Justice

with regard to the answer to be given to the question referred to us."

(Emphasis supplied)

20. In ***AMD Metplast Pvt. Ltd.*** (*supra*) this court taking into account the above judgment and the peculiar facts and circumstances of the case inter alia held that consideration in the form of commission which was paid to Ashok Gupta was for services rendered by him as per terms of appointment as a Managing Director.

21. For the proper understanding, it is necessary to refer to the facts in ***AMD Metplast Pvt. Ltd.*** (*supra*). In this case Ashok Gupta was the Managing director of the appellant company and was paid commission of Rs.25 lakhs. There was an agreement dated 1st April, 1997 between Ashok Gupta and the appellant company and under this agreement, Ashok Gupta was entitled to salary of Rs.30,000/- per month and commission @ 1% of the annual turnover of the company in case it achieves annual sales of Rs.10 crores. In case of a shortfall, the commission was payable @ 0.5%. The agreement was valid upto 31st March, 2022. Thereafter, by the resolution passed by the Board of Directors dated 18th June, 2002 it was agreed that Ashok Gupta, Managing Director would be paid commission of 1% of the sales subject to a ceiling of Rs.25 lakhs. Ashok Gupta was also paid salary of Rs.7,20,000/-.

22. On the basis of the facts, the tribunal in this case had observed that Ashok Gupta had 9.98 % of the paid up share capital and the assessing officer had observed that appellant company had earned net profit of Rs.1,20,03,950/- but had not paid any dividend. However, commission of Rs.25 lakh was paid to Ashok Gupta. In the appeal before the High Court,

the High Court took a view that as per the terms of employment Ashok Gupta was entitled to receive commission for services rendered to the company. The commission was treated as part and parcel of the salary and TDS had been deducted. Thus, the factual matrix of present case and ***AMD Metplast Pvt. Ltd.*** (*supra*) are totally different.

23. If we take the analogy in case of ***Loyal Motors Service Company Ltd.***(*supra*) also, the basic object of Section 36 (1) (ii) is intended to prevent an escape from taxation by describing a payment as bonus. The simple test is that had the bonus or commission not been paid, it would have added to the profits or dividend of the company. Thus, the deduction is permissible only if the sum paid is bonus or commission for services rendered.

24. In the present case, there is not even an iota of word that the amount paid is commission for services rendered or bonus.There are only two directors in the company. The entire amount has been paid to both of them. It is not the case of the appellant that there has been any term of employment nor is there any case that any special services has been rendered by these two directors. On the similar analogy, the judgment in Career Launcher Ltd. (supra) is also distinguishable. In ***Career Launcher Ltd.*** it was *inter alia* held as under:

> *"19. The revenue's contention that the Tribunal erred in allowing the bonus payment to the directors cannot be accepted. It has not disputed the facts viz., (a) that the payment was supported by board resolutions and (b) that none of the directors would have received a lesser amount of dividend than the bonus paid to them, having regard to their shareholding. Further, the directors are full-time employees of the company receiving salary. They are all graduates from IIM, Bangalore. Taking all these facts into consideration, it would appear that the bonus was a reward for their work, in addition to the salary*

> *paid to them and was in no way related to their shareholding. The bonus payment cannot be characterised as a dividend payment in disguise. The Tribunal hasfound that having regard to the shareholding of each of the directors, they would have got much higher amounts as dividends than as bonus and there was no tax avoidance motive. The quantum of the bonus payment was linked to the services rendered by the directors. It cannot therefore be said that the bonus would not have been payable to the directors as profits or dividend had it not been paid as bonus/commission.*
>
> *20. The issue has been considered by this Court in AMD Metplast Pvt. Ltd v. DCIT (2012) 341 ITR 563 in the light of the judgment of the Bombay High Court in Loyal Motor Service Co. Ltd v. CIT (1946) 14 ITR 647. It was observed that the judgment of the Bombay High Court (supra) does not assist the revenue and that so long as the bonus or commission is paid to the directors for services rendered and as part of* their terms of *employment it has to be allowed and sec.36(1)(ii) does not apply*."

25. The conclusion as reached in the ***CIT v. Career Launcher India Ltd.*** 358 ITR 179 (Del) was as long as the bonus or commission is paid to the directors for services rendered and as part of their term of employment, it has to be allowed.

26. We consider that the question of law is very well settled. There is no substantial question of law in the present cases. The assessing officer and CIT (A) have given a concurrent finding that the assessee has paid the bonus in lieu of the dividend and therefore, the above sum is disallowed under Section 36 (1) (ii) of Act. The ITAT also after considering the findings of the assessing officer and the CIT (A) had *inter alia* held that the payment of bonus or commission is not allowable as deduction under Section 36 (1) (ii) of the Act in the hands of the assessing company. In the absence of any

substantial question of law, the appeals are liable to be dismissed. Hence, the present appeals along with the pending applications are dismissed.

DINESH KUMAR SHARMA, J

MANMOHAN, J

APRIL 13, 2022
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