IN THE INCOME TAX APPELLATE TRIBUNAL
VISAKHAPATNAM BENCH, VISAKHAPATNAM

BEFORE SHRI V. DURGA RAO, HON'BLE JUDICIAL MEMBER &
SHRI D.S. SUNDER SINGH, HON'BLE ACCOUNTANT MEMBER

ITA No. 340/VIZ/2016
(Asst. Year : 2012-13)

DCIT, Circle-4(1), Visakhapatnam.	vs.	M/s. Sri Varalakshmi Jute Twine Mills Pvt. Ltd., Bobbili Road, Rajam (PO), Srikakulam District. PAN No. AADCS 1167 L

ITA No. 349/VIZ/2016
(Asst. Year : 2012-13)

Sri Varalakshmi Jute Twine Mills Pvt. Ltd., Bobbili Road, Rajam (PO), Srikakulam Dist. PAN No. AADCS 1167 L	vs.	ITO, Ward-3, Srikakulam.

ITA No. 458/VIZ/2017
(Asst. Year : 2013-14)

ACIT, Circle-4(1), Visakhapatnam.	vs.	M/s. Sri Varalakshmi Jute Twine Mills Pvt. Ltd., Bobbili Road, Rajam (PO), Srikakulam District. PAN No. AADCS 1167 L

ITA No. 404/VIZ/2017
(Asst. Year : 2013-14)

Sri Varalakshmi Jute Twine Mills Pvt. Ltd., Bobbili Road, Rajam (PO), Srikakulam Dist. PAN No. AADCS 1167 L (Appellants)	vs.	DCIT, Circle-4(1), Visakhapatnam. (Respondents)

Assessee by	:	Shri Yogesh A. Thar & Shri Sunil Jain – CAs.
Department By	:	Shri T. Satyanandam – Sr.DR
Date of hearing	:	04/01/2018.
Date of pronouncement	:	09/02/2018.

O R D E R

PER V. DURGA RAO, JUDICIAL MEMBER

ITA Nos. 340 & 349/VIZ/2016 are the cross appeals filed by the revenue and the assessee against the order of Commissioner of Income Tax (Appeals)-2, Visakhapatnam, dated 28/04/2016 for the Assessment Year 2012-13.

ITA Nos. 458 & 404/VIZ/2017 are the cross appeals filed by the revenue and the assessee against the order of Commissioner of Income Tax (Appeals)-2, Visakhapatnam, dated 25/05/2017 for the Assessment Year 2013-14. Since, the issues involved in these appeals are common, clubbed and heard together and are disposed of by this consolidated order.

ITA No.340/VIZ/2016

2. Facts of the case, in brief, are that the assessee is a private limited company, filed its return of income admitting total income of Rs. 17,91,004/-. The return filed by the assessee was processed under section 143(1) of the Income Tax Act, 1961

(hereinafter referred to as 'Act') and after following due procedure, assessment is completed under section 143(3) of the Act by disallowing expenses claimed by the assessee of Rs.1,63,76,644/-. The assessee-company was incorporated on 27/06/1978 in the name of Sri Vasavi Jute Twine Mills Pvt. Ltd. and was engaged in the business of manufacturing jute. Subsequently, the assessee-company got amalgamated with M/s.Sri Lakshmi Jute Twine Mills under the scheme of amalgamation and subsequently, it got engaged in operating and managing two jute mills namely, Sri Vasavi Jute Twine Mills Pvt. Ltd. and M/s. Sri Varalakshmi Jute Twine Mills. The name of the company was changed to M/s. Sri Varalakshmi Jute Twine Mills in the year 1991. The assessee-company leased out to Sri Vasavi Jute Twine Mills Pvt. Ltd. w.e.f. 06/11/1998 for the first time. Thereafter, it was being leased out to different lessees. With effect from 01/09/2004, the company leased out to Sri Varalakshmi Jute unit also. The lease rentals from the two units have been offered to tax as income from business. During the subject year, Sri Vasavi Jute Twine Mills Pvt. Ltd. was leased out to M/s. Nidhi Jute Mills and Sri Varalakshmi Jute Mills was leased out to M/s. Howrah Mills Company Ltd. In the assessment order,

the Assessing Officer has noted that the assessee-company has claimed substantial expenses towards employees' benefits to the tune of Rs. 1,76,65,226/-. The details of such expenses were explained to the Assessing Officer as under:-

Sl. No.	Expenses Details	Amount (Rs.)	Total Amount (Rs.)	Remarks
1.	Salaries, wages and bonus etc.		15,82,206	Payment made to the existing employees of the company
2.	Contribution to Provident Fund (PF)		18,176/-	This represents the amount of employer contribution to PF made with respect to the existing employees.
3.	Staff Welfare Expenses			All these payments represent payment made to Former employees of the Company working with it and which are presently continuing their service with the lessees to whom the assessee has leased out both the Jute Mills.
(i)	Paid to Mr. Appa Rao for expenses on Medical treatment	48,000		The said payment represents payment made for the expenses on medical treatment of Mr Appa Rao, a former worker of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company.
(ii)	Paid to G. Bhushana Rao for staff expenses	4,800		The said payment represents payment made for the expenses on medical treatment of Mr.G.Bhushana Rao, a former workmen of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company.
(iii)	Payment of Medical	17,626		The said payment

	Insurance for the workers of Varalakshmi Unit			represents payment made for medical insurance to United India Insurance company for carrying out group medi-claim for the workmen of Sri Varalakshmi Jute Mills which have been leased Out to M/s Howarh Mills Company Limited.
(iv)	Paid to SV Diwakara Rao, ex-employee, for expenses on Medical treatment	35,000		The said payment represents payment made for the expenses on medical treatment of Mr S.V. Diwakara Rao, a former workmen of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company.
(v)	Paid to B. Maralidhar (for daughter's marriage)	5,000		The said payment represents payment made at the occasion of daughter marriage of Mr B. Muralidhar a former associate of Sri Varalakshmi Jute Mills.
(vi)	Paid to B. Ramesh Babu for expenses on Medical treatment	48,000		The said payment represents payment made for the expenses on medical treatment extended by Dr. B. Ramesh to the workers/ staff of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company.
(vii)	Lump sum ex-gratia payment made in addition to regular festival bonus/ex-gratia payment to the workmen of Sri Vasavi Jute Mills	97,47,082		Lump sum ex-gratia payment made to the workmen of Sri Vasavi Jute Mills have been intimated to the present employer M/s. Nidhi Jute Mills to consider the same as part of their salary for the purpose of deduction of TDS wherever applicable, in accordance with the provision of section 192 of the Income-tax Act, 1961.
(viii)	Ex-gratia function expenses	79,540		These expenses were incurred for the lumpsum Ex-gratia distribution function held on 13-01-2012

				an the details of expenses under various heads suchsnacks, tea, coffee, rent for chairs, pendal, photograph expenses etc.
(ix)	Varalakshmi Jute Mills workers children education	8,500		The said payment represents payment made towards expenses on education of former workmen which a currently working with Sri Varalakshmi Jute mills lease out to by the assessee company to M/s. Howarh Mills Company Limited.
(x)	Cycle for office boy	3,200		The said payment represents payment made for expenses towards the cycle provided to Office Boy of the company.
(xi)	Payment made to Mr. Surabhi Satish, an ex-worker to support expenses on the marriage of her dependent-sister	1,00,000	1,00,96,748	The said payment represents payment made to Surabhi Satish, a Former associate of the Company. Financial help is extended by the company against the representation received from the associate.
4	Payment of periodical festival bonus and ex-gratia to the workmen/staff of Sri Vasavi Jute Mills and Sri Varalakshmi Jute Mills		27,59,958	This represents payment made towards periodical festival bonus/ex-gratia to the workmen/staff of Sri Vasavi Jute Mill and M/s. Sri Varalakshmi Jute Mill Units which are leased to M/s. Nidhi Jute Mills and M/s. Howarah Mills Company Ltd., respectively during the assessment year under consideration.
5.	Allowance for children education		31,44,132	This represents payment made towards the education of the children of the workmen of Sri Vasavi Jute Mill and M/s.Sri Varalakshmi Jute Mill units which are leased out to M/s. Nidhi Jute Mills and M/s. Howrah Mills Company Ltd., respectively during the assessment year under consideration
6	Other staff welfare expenses		64,006	Other Welfare expenses
	Total		1,76,65,226	

3. In the assessment order, the Assessing Officer has noted that most of the above expenditure, except item No.1 of the above table, were incurred in relation to workmen of Sri Vasavi Jute Mill and Sri Varalakshmi Jute Mill, which were leased out to M/s. Nidhi Jute Mills and Howrah Jute Mills Company Ltd. Therefore, the Assessing Officer called upon the assessee to justify the allowability of such expenditure under section 37 of the Act. In response to the query raised by the Assessing Officer, the assessee filed a detailed submissions before the Assessing Officer in respect of expenditure claimed by it, which is reproduced as under:-

> *"We have been required to state and produce evidence for such payments and under which agreement these payments were made, whether any TDS was made on such ex-gratia payments, further justify the claim of expenses as per lease agreement etc.*
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> *At the outset, we would like to submit that the payment debited under heading "Employee Benefit expenses" represents payment made to existing as well as former employees of the assessee company who have worked with the assessee company when it was running the Jute mills by itself and such workmen have continued their services with the lessee(s) of the assessee company whom the assessee has leased out the jute mills from time to time. In terms of lease agreement entered into with the different lessees(s), the present wages payment for the services rendered while the lease is continuing their obligation While, the payment of periodical festival bonus/ex-gratia at the time of Pongal, expenses to meet the expenses on education of the children of the workmen under a scheme framed by the assessee company for making such payment and support for the dependent children / family members marriage, etc., wherever necessary, is a contractual obligation of the assessee towards the workmen of Sri Vasavi Jute Mills and Sri Varalakshmi Jute Mills as well as payment of lumpsum ex-gratia payment to meet the expectation of workmen of getting such lumpsum*

amount for their long services with the assessee company as well as continuing their services with the different lessee(s) to who whom the jute mills were leased out from time to time, as committed by the management of the assessee company at the time of discontinuing the running of jute mills by itself remains the contractual obligation of the assessee company as would be evident from the submissions with supporting documents for incurring such payments vis-à-vis the details of such payments made in earlier years and allowed as deduction in the assessment of the company, made hereunder. In view of the this, there is a contractual liability of the assessee to make payment of periodical festival bonus /ex-gratia, supports children education of the workmen in terms of the company's scheme for making payment of such amounts ever after leasing out the jute mills in order to have continuity of the employees in business interests, maintain good relations with the employees, to buy industrial peace and save the running of jute mill leased, from strikes and lock-outs, etc. as there is a continuous labour problem of skilled labour in the industry and its is difficult to get the skilled labour as and when the unit needs them. Had the workmen not continued with the assessee company and with its different lessee(s) to whom the jute mills were leased out from time to time, it was not possible for the assessee company to lease out the jute mills and earn lease rental income on regular basis from such leasing of jute mills with workmen. Thus all the amounts being expended by the assessee company towards 'Employee Benefit expenses: were in the business interest and on the ground of commercial expediency and in order to directly facilitate the continuity as well as carrying on the leasing business and earning leased rental income on regular basis from such leasing of jute mills and hence the said amounts were incurred wholly and exclusively for the purpose of business".

4. The Assessing Officer has considered the above explanation and observed that there was a labour unrest in the assessee's company in the year 1998, during which the assessee-company proclaimed 'lock-out' of the factory on 20/02/1998 and also retrenched the services of 220 workmen by paying compensation. During the pendency of the conciliation proceedings before the Dy.Commissioner of Labour, the assessee-company transferred

the factory by way of lease on 06/11/1998 to Mahadev Jute Mills. The Industrial Tribunal-cum-Labour Court upheld the 'lock-out' declared by the management and also held that the termination of services of 220 workmen by invoking provisions of section 25FF was justified. The said order was challenged before the Hon'ble High Court of Andhra Pradesh, which is said to be pending. As per the affidavit filed before the Hon'ble High Court, there were nearly 370 workmen and 70 apprentices in the assessee-company. On the intervention of the District Collector all these workmen, who were terminated by Sri Vasavi Jute and Twine Mills Pvt. Ltd., except the apprentices were provided employment by the lessee company. With reference to this information, the Assessing Officer took a view that once services of the employees were terminated and their terminal benefits have been paid by the lessee company, they could no longer be considered as employees of the assessee-company, and that the assessee company could not be considered to be under any legal obligation to pay any compensation, bonus, ex-gratia, salary and wages to those employees and these expenses are supposed to be incurred by the lessee company.

5. The Assessing Officer further observed that two leases commenced from 01/09/2010 and supposed to continue till 31/08/2016. For the Financial Year 2011-12, relevant to the Assessment Year 2012-13, other than 12 regular employees to manage and control, the only source of income 'lease rentals' and to attend the related works, as claimed by the company, the other persons, who are stated to be ex-employees or workmen are not at all related to lesser company i.e. assessee and as per clause-v of lease agreements, for this period under consideration, the lessee has to borne every expenditure of company's employees, and hence, the subject expenditure claimed is an allowable expenditure in the hands of the assessee company, since it is not assessee's obligation and necessity to make such payments and the expenditure incurred is not in relation to the present business of the assessee –company. Thus, the Assessing Officer noted that as per the lease agreement, there is no obligation on the part of the assessee's company to make payment of periodical festival bonus/ex-gratia/support to children education of the workmen and payment of medical expenses etc. The Assessing Officer further noted that there was no contractual liability on the assessee to make these payments. The Assessing Officer also noted that

assessee failed to produce any documents to show that contractual obligation existed between the assessee-company and the ex-employees to make such payments as obligatory. The Assessing Officer further opined that none of the former employees/ex-employees are in relationship of employer and employee with the assessee. Besides, as the assessee company had already paid retrenchment benefits and other terminal benefits, there is no question of payment of further benefits to those employees, who are already terminated. Therefore, the expenditure incurred by the assessee is not an allowable deduction under section 37 of the Act. The assessee has contended before the Assessing Officer that similar expenditure claimed towards festival bonus, children allowance in the earlier years has been allowed and therefore this year also, no disallowance can be made. The Assessing Officer has observed that the similar payments were already made in the earlier years have been accepted under section 143(1) of the Act for the Assessment Years 2010-11 & 2011-12, for the Assessment Year 2009-10 order was passed under section 143(3) of the Act. The Assessing Officer took the view that each assessment year is separate proceedings and the issues have to be dealt with as to

the facts and evidence during the assessment proceedings. The Assessing Officer also noted that this is the first year, the assessee has claimed ex-gratia payments of lump-sum amount of Rs. 97.47 lakh to its employees. Therefore, the decisions taken in the Assessment Years 2009-10, 2010-11 & 2011-12 are different and have no application to the year under consideration. Accordingly, the Assessing Officer has disallowed the expenditure claimed by the assessee of Rs. 1,63,76,644/-.

6. The Assessing Officer further noted that even if assessee's plea regarding payment to ex-employees had to be accepted, only employees who were on the assessee's roll on 20/02/1998 and employed with lessee as on 13/01/2012 being the date of payment of ex-gratia, could be considered eligible for such ex-gratia payment. Considering this fact, the Assessing Officer noted that the persons with service between 10 to 11 years, would not be eligible for any ex-gratia payment and more specifically the employees referred to at serial Nos. 114, 116, 173 to 182, 184 to 187, 189 to 195, 197 to 200, 202 to 220, 232, 234, 235, 241 and 246 would not be eligible for the subject payment.

7. On being aggrieved, the assessee carried the matter in appeal before the ld. CIT(A). Before the ld. CIT(A), the assessee has filed a detailed submission along with details of the employees and payments made to them. The ld. CIT(A) has considered the issue and categorised the payments as under:-

a) Children education allowance of Rs. 31,44,132/- and festival bonus of Rs. 27,59,958/-, aggregating to Rs.59,04,090/-

b) Other payments of Rs. 4,25,472/- have been disallowed.

c) Lumpsum ex-gratia payment of Rs. 97,47,082/-

8. So far as expenditure incurred towards ex-gratia bonus, allowance of children education, the ld. CIT(A) has allowed Rs.30,21,192/- and Rs. 27,55,458/- and for remaining balance, he confirmed the order of the Assessing Officer. The assessee has submitted mainly before the ld. CIT(A) that the payments made to the ex-employees is a prior agreement i.e. before the date of leased out the factory to the lessee. Therefore, it is the commitment made by the assessee to the ex-employees and accordingly payment is made. It is also submitted that the payments made by the assessee are in the business expediency, hence, allowable under section 37 of the Act. It is also submitted

that the genuineness of the payments made by the assessee are not doubted by the Assessing Officer and submitted that the entire expenses claimed by the assessee have to be allowed. The ld.CIT(A) after considering the explanation of the assessee and also by considering various judicial pronouncements, allowed children education allowance of Rs.30,21,192/- and Rs.27,55,458/-. The relevant portion of the order is extracted as under:-

> *"6. I have gone through the written submissions filed by the authorized representative vide letters dated 21.09.2015, along with factual paper book and legal paper book dated 23.12.2015 and 04.02.2016 and case law paper book, dated 28.12.2015 along with details filed and the submissions made during the course of hearing; the written submissions filed along with details, and also the submissions of the AO. I have also gone through the assessment record and the information contained therein. The decisions relied on were also considered and based on these various issues raised in the appeal are adjudicated.*
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> *7. The issues that arise in the above narrated factual matrix would be whether the impugned payments made in the form of children education allowance, festival ex-gratia payments, other ex-gratia payments and lump sum ex-gratia are allowable as deduction u/s.37(1) of the I T Act. It is relevant to note that the children education allowance and festival ex-gratia payments were said to be made year on year; whereas the lump sum ex-gratia payment were made for the first time and in two installment. It has to be seen whether the impugned payments arise out of contractual obligation as contended and whether the impugned payments could be allowed as deduction on the grounds of commercial expediency or business expediency. It is also relevant to note that the genuineness of the payments are not questioned. The payments may categorized as under:*
>
> a) Children education allowance (Rs.31,44,132/-) & festival bonus (Rs.27,59,958/-) aggregating to Rs.59,04,090/-
> b) Other payments disallowed (Rs.4,25,472/-).
> c) Lumpsum exgratia payment of (Rs.97,47,082/-).

8. <u>Expenditure incurred towards Ex-gratia bonus, allowance of children education (Rs.27,59,958 + Rs.31,44,132):</u>

8.1 During the appeal hearing, the authorised representative submitted the total amount disallowed, an amount of Rs. 31,44,132/- represent payment towards education of children of workmen of Vasavi Jute Mill & Sri Varalakshmi Juite Mills, and that an amount of Rs. 27,59,958/- was incurred towards periodical festival bonus/Ex-gratia to workmen/staff of Vasavi Jute Mill and M/s. Varalakshmi Jute Mill. A copy of the note on the deductibility of the said expenditure along with the Board resolution and copy of the policy statement/ scheme of the company which were submitted to the AO was filed for consideration. The list of workers to whom the payment was made was filed in the form of two booklets and details of payment made in the earlier five years were also submitted. The authorised representative further represented that these payments are made year upon year right from 1998, and has filed copies of financial statements of the company. It was stated that copies of audited accounts from F.Y.2002-03 to F.Y.2011-12 were submitted to the AO. It was represented that the periodical festival bonus/ ex-gratia and children education allowance were paid to the workmen of Vasavi & Varalakshmi Jute Mills right from date of start of unit and after leasing out with a view to improve the morality and efficiency of the workers and for smooth operations of the lease. It was submitted that the TDS on the payments have been effected by the lessees. The authorised representative also submitted that the assessee had offered the impugned payments for the purpose of FBT from A.Y.2006-07 to A.Y.2009-10. It was further submitted that the assessee had claimed these amounts as business deduction in the earlier years and was allowed by the Department. It was submitted that for the A.Y.2003-04 & A.Y.2009-10 the AO had completed assessment u/s.143(3) and has accepted the deductibility of these expenses as business expenditure u/s.37 of the I T Act, and copies of the assessment orders for A.Y.2003-04 and A.Y.2009-10 were filed. It was contended that the claim was consistently allowed by the Department in the earlier years and that disallowance has been made for the first time this year which was not justified and was not in accordance with the principle laid down by the Hon'ble Supreme Court in the case of Radhasoami Satsang vs. CIT (193 ITR 321). The authorised representative also contended that the principle of consistency should be followed by the AO and relied on the following decisions:

(i)	*Radhasoami Satsang vs. CIT (193 ITR 321) (SC)*
(ii)	*CIT vs. ARJ Securities Printes (264 ITR 276)(Del*
(iii)	*CIT V. Neo Poly Pack (P) Ltd (245 ITR 492) (Del)*
(iv)	*Burmah Shell v. Chand (61 ITR 493) (Born);*
(v)	*Royal Business Centre Pvt Ltd v ITO (39 BCAJ 24) (Born);*
(vi)	*CIT v Godavari (156 ITR 835) (MP);*
(vii)	*Namozil v CIT (174 ITR 58) (Mad); and*
(viii)	*CIT v Neo poly pack (P) Ltd. (245 ITR 492) (Del)*

8.2 Thus, it was contended that the year on year payment which have been accepted and allowed as deduction in the earlier assessment years in the case of assessee company should be allowed as deduction based on principles of consistency in view of settled legal position as stated above. The authorized representative also contended that the impugned payments were made as part of its contractual obligation as referred in the scheme and with a view to have good relations with the workmen and their continuity of services with the lessees whom the assessee has leased out the Jute Mills from time to time. It was contended that ex-gratia bonus was incurred to fulfill the expectation of the workmen of getting periodical festival bonus/ ex-gratia on continuous basis as committed to them by the management when they were working with it when it was operating the jute mills by itself and extended such facility when the mills were leased out. The authorised representative asked to clarify with reference to the lease agreement entered with the lessee as to which of the employee welfare payments were the responsibility of the lessee, and whether the impugned payments were the responsibility of the lessee under the lease agreement. The authorised representative was also asked to clarify as to whether impugned payments were claimed as deduction by the lessee. In response the authorised representative filed reply vide letter dated 04.02.2016 wherein it was stated as under:

a) *Till the year 1998, the Appellant was running Sri Vasavi Jute itself and it leased out the foresaid unit to Mahadev Jute Mills for running and operating the same. The Appellant made available workmen and staff for running and operating the aforesaid unit to the lessee. Further, the Appellant in the year 2004 decided to lease out Sri Varalakshmi Jute Unit to M/s Howarh Jute Mills Company Limited on lease. The Appellant made available the workmen and staff for running and operating the foresaid unit by the lessee during the lease period.*

b) *In terms of the understanding, arrangement and the lease agreement entered into with the lessee, the lessee is responsible to pay the amount of wages for the period of service rendered by the workmen, terminal benefits such as Provident fund, ESIC, Statutory Bonus as per payment of Bonus Act and the amount of Gratuity as per the payment of Gratuity Act 1972 and also liable to make payment of retrenchment compensation in case of any retrenchment of any of the workmen happens, during the lease period. The lessee was not liable to make any payment towards Children Education Assistance to the Workmen and their Children and the periodical Ex-gratia payment at the time of Pongal festival, any medical treatment expenses and / or any lump sum ex-gratia payment to the Workmen/Staff. As per the understanding and arrangement between the Lessee as well as the workmen employed in the aforesaid two units, the responsibility to make payment of Children Education Assistance to the Workmen and their Children and the periodical Ex-gratia payment at the time of Pongal festival, any medical treatment expenses was the contractual obligation of the Appellant with a view to have good relations with the workmen, smooth running of jute unit, their continuity with the lessee to whom the Jute units were leased out from time to time, so as to*

ensure earning of the regular lease income.

c) *Thus the payment of Children Education Assistance to the Workmen and their Children and the periodical Ex-gratia payment at the time of Pongal festival, any medical treatment expenses in terms of the understanding and arrangement with the lessee and the workmen working with the aforesaid two jute units was contractual obligation of the Appellant under the scheme framed for this purpose on year on year basis. In other words, the responsibility of making aforesaid payments was that of Appellant and the Lessees were only responsible to make payment of wages for the period of service and the terminal benefits and retrenchment compensation as stated above.*

d) *The Lessee has neither debited the aforesaid payment in their books of account nor they have claimed any deduction of same in their return of income. In support of above, confirmation dated February 4th, 2016 from the Lessee, namely Mahadev Jute Mills is enclosed herewith in Anneuxre-1.*

e) *It is submitted that the appellant has implemented Children Education assistance scheme under which it is providing support of the Children of Workmen/Staff working in the aforesaid unit, based on the criteria/ procedure stated in the scheme which is framed on year to year basis.*

f) *It is further submitted that the amount of Children Education assistance is either directly paid by the Appellant to the schools / institutions where the Children of the workmen are studying or in those cases where workmen have already paid such expenses the appellant is making reimbursement of expenses in terms of the aforesaid scheme. However there are cases where the amount was initially paid by the Lessee viz., Howrah Jute Mills Ltd in order to facilitate timely payment of fee by the Workmen and in terms of the understanding and arrangement the same was recovered / reimbursed from the LESSOR viz., Sri Varalakshmi Jute Twine Mills Pvt. Ltd.*

g) *It is submitted that during the previous year 2011-12 MIs Howrah Jute Mills Limited has initially paid in towards Children Education Assistance in respect of the Workmen/Staff working in the aforesaid unit and later on recovered the aforesaid amount from the Lessor i.e Appellant. In support of the above the copy of ledger account evidencing the payment as well as recovery of the aforesaid amount initially paid towards Children Education Assistance scheme is attached to this letter.*

8.3 *It was contended that once the employer-employee relationship is established then it continue forever. As per Section 15 r.w.s. 17 of the I T Act, any of the payment made by the employer or former employer to the employee would be taxed in the hands of the employee as salary income only, and therefore such expenditure should be allowed in the hands of the employer as salary expenditure. It was also contended that these payments have suffered FBT, which has been accepted by the*

department and therefore the said expenses cannot be disallowed u/s.37(1) of the Act, and, in this regard, reliance was placed on the decision of Hon'ble Mumbai Tribunal in the case of Hansraj Mathurdas vs. ITO (ITA No.2397/M/2010). It was further contended that even if there is no employer - employee relationship, such payments are allowed as deduction on the basis of commercial considerations. It was submitted that there were various judicial decisions where payments made to former employees or the relatives of the deceased employees in the nature of pension were allowed as deduction; and reliance was placed on the decision of Hon'ble Madras High Court in the case of CIT vs. Lucas Indian Service Ltd. (239 ITR 429), Hon'ble Gujarat High Court in the case of CIT vs. Laxmi Cement Distributors (P) Ltd. 104 ITR 711; Hyderabad Tribunal decision in the case of A.P. Housing Board vs. DCIT (36 Taxmann.com 561), Cochin 1TAT in the case of Catholic Syrian Bank Ltd. vs. ACIT 38 SOT 553.

8.4 The authorized representative relied on the decision of the Hon'ble Supreme Court in the case of CIT v Chandulal Keshavlal & Co. (38 ITR 601 (SC)) and contended that expenditure incurred on the ground of commercial expediency and in order indirectly to facilitate the carrying on of the business is allowable. It was contended that the fact that there was no compelling necessity to incur the expenditure on which deduction is claimed is irrelevant to constitute expenditure under section 37(1) of the Act, and that in every case it is a question of fact whether the expenditure was incurred wholly and exclusively for the purpose of trade or business. The authorised representative referred to the various tests laid down by the Hon'ble Gujarat High Court in CIT vs. Navasari Cotton and Silk Mills Ltd. (135 ITR 546) and submitted that the assessee satisfies the positive tests and that none of the negative tests are attracted. The authorised representative contended that the rule that increased remuneration can only be justified if there be corresponding increase in profits of the employer is erroneous and relied on the decisions of Supreme Court in the case of CIT vs. Walchand & Co. (P) Ltd. (65 ITR 381 SC), and Travancore Titanium Products vs. CIT (60 ITR 227 (SC)). It was submitted that expenditure incurred voluntarily on the ground of commercial expediency and in order indirectly to facilitate the carrying on of the business may yet be expended wholly and exclusively for the purpose of the trade CIT vs. Delhi Safe Deposit Co. Ltd. (13 ITR 756 SC); CIT vs. Sales Magnesite P Ltd. 214 ITR 1; CIT vs. Panipat Woolen & General Mills Co. Ltd. 103 ITR 66 SC; CIT vs. Associated Electrical Agencies 266 ITR 63 (Mad); Udaipur Distillery Co. Ltd. 224 CTR 32 SC; Adidas India Marketing P Ltd. 10 Taxmann.com 18. It was contended that expediency of the expenditure is not for the Revenue to consider and relied on the decision of Hon'ble Madras High Court in Amarjothi Pictures vs. CIT 69 ITR 755, and CIT vs. Gobald Motor Services P Ltd. 100 ITR 240 (Mad). It was pointed out that the question of commercial

expediency has to be decided from the point of view of businessman and not by the subjective standard of reasonableness of revenue as held by Bombay High Court in CIT vs. Sales Magnesite P Ltd. 214 ITR 1 and CIT vs. Dalmia Cement 254 ITR 377 SC, CIT vs. Dhanraj Giriji Raja Narsinginji 94 ITR 544. It was also contended that contractual obligation and legal liability are not the touch stone to test commercial expediency, and relied on the decision in the case of CIT vs. Associated Electrical Agencies 266 ITR 63, CIT vs. Motor Industries Co. Ltd. 223 ITR 112 (Kar.), Udaipur Distillery Co. Ltd. 224 CTR 32 SC. The authorised representative also referred to the observation of Hon'ble Supreme Court in the case of Bengal Enamel Works Ltd. (77 ITR 119), stating that the Revenue authority cannot substitute its own view of how the assessee's business affairs should be managed. Thus it was contended that the periodical festival bonus/ ex-gratia and children educational allowance were incurred under a scheme as part of assessee's contractual obligation committed to the workmen while discontinuing the operation by itself, and the expenditure was incurred in order to facilitate running of its business and towards interests of assessee's business and are to be allowed u/s. 37 of the IT Act.

8.5 In brief, the contentions of the assessee can be summerised as under:-

a) *Payments were made as part of contractual obligation under the scheme.*
b) *Payments were made as per scheme approved by the management and sanctioned by the Board of Directors.*
c) *Ex-gratia/bonus paid when the assessee was operating the mills and commitment given to the employees that these facilities will continue even after the lease of mills give rise to expectation of employees that they would be entitled to these benefits.*
d) *Payments were made year on year, and was allowed by the Department in all the earlier years, and thus the principle of consistency should be followed.*
e) *Payments were made to maintain good relations with workers, to buy industrial peace and to save the running of Jute Mills lease from strikes and lockouts etc.*
f) *Payments were made on grounds of commercial expediency/ business expediency for continuity of regular lease income and to protect assessee's business interests.*

8.6 From the perusal of Board resolution as per minutes of Board meeting dated 15.06.2011, it is seen that the company had agreed to pay children education allowance to the workers and staff of the units of Sri Vasavi and Sri Varalakshmi as per policy adopted by the company and as per practice adopted every year with a view to have good relations with the workers and staff of Sri Vasavi and Sri Varalakshmi unit of the

company. Relevant extract of the Scheme narrates as under:

PREAMBLE:

It was recognized by the Company, Sri Varalakshmi Jute Twine Mills Pvt. Ltd., that providing educational assistance to the children of the workers of Vasavi and Sri Varalakshmi Units is very essential as the workers with meagre income could not extend education to their children and there by the future of the children and the dreams of the parents will be vanished if timely support is not given for the education. Though the Units were given on lease, the Management of SVJTMPL felt it necessary to provide the education assistance to its ex-workers of Sri Vasavi and Sri Varalakshmi Units for a smooth functioning of the Company. Hence, preference was given for the children education of the workers so that the workers need not worry about the education of their children as the Company takes care of the activity and can concentrate on the work, which in turn will help for smooth operations of lease and to improve the morality of the workers and will help to improve the efficiency of the workers.

FEATURES OF THE SCHEME:

1. *All the workers and staff of Vasavi and Varalakshmi Unit Workers*
2. *The employee should complete one year of minimum service to be eligible for assistance*
3. *Assistance is restricted to 2 children per employee*

As per the scheme, Rs. 17,84,078/- paid to workers and staff of Sri Varalakshmi Unit, and Rs. 9,78,880/- was paid to Sri Vasavi Unit.

8.7 From the perusal of the Board resolution as per minutes of Board meeting dated 04/10/2011 the company agreed to pay the periodical festival bonus/ ex-gratia for pongal to workers and staff of units of Sri Vasavi and Sri Varalakshmi as per the practice adopted by the company with a view to have good relations with the workers and staff of Sri Vasavi & Sri Varalakshmi units of the company. Relevant extract of the scheme filed, narrates as follows:-

PREAMBLE:

With a view to improve the morality and efficiency of the workers and for smooth operations of lease, the management of Sri Varalakshmi Jute extends the payment of exgratia to its ex workers of Vasavi and Sri Varalakshmi Units every year as per the policy and procedure as under:

POLICY:

1. *Committee consisting of Director, Plant Managers of the Units, and Two Local Officials will discuss the issues raised by the both units union members and keeping in view of previous year experience, proposed the following policy:*
2. *All workers and staff working in Vasavi and Varalskhmi Jute Units are covered under the scheme.*
3. *Festival Bonus / Ex-gratia covers the period from*

December 2010 to November 2011.

4. *Every employee has put in 240 days of service, including leave on account of accident, maternity leave, etc.*
5. *Employee has to complete one year of service to become eligible for the Ex-gratia. (changed from the existing stipulation of six months minimum service)*
6. *Minimum Ex-gratia is fixed at Rs. 700/- per employee.*
7. *Ex- Vasavi (INTUC) workmen working in our unit, whose attendance is below 240 days, will be paid Rs.1000/- each, on par with the Ex-Vasavi (INTUC) workmen working outside.*
8. *Other category workers not considered for Exgratia, if the attendance is below 240 days.*

Policy stipulations 1 to 4 are normalized for both the units.

As per Scheme Rs.24,35,366/- paid to Varalakshmi workers and Rs.5,67,826/Varalakshmi workers.

8.8 The perusal of the Scheme and payment details reveal that ex-gratia bonus payments made for Ex-vasavi (INTUC/ C1TU) employees, Nldhi Jute Mill workers and staff, Varalakshmi Jute Mill workers before and after leased out taking into account the number of working days, the number of years of service and their salary structure. The scheme of children education allowance has taken into account the salary structure and the level of education.

8.9 During the appeal hearing, it was claimed that the assessee has been incurring these expenditure right from the start of the unit. The assessee filed copy of financial statements as on 31.03.1999 onwards, and pointed out that expenditure has been claimed towards 'bonus' and 'welfare expenditure' as could be seen in its profit and loss account. I have perused the details filed. It is seen that in the profit & loss account for the year ended 31/03/1999 to 31/03/2006, expenditure has been debited towards 'bonus' & 'welfare expenditure'. On the other hand, in the P & L account for the years ended 31/03/2007 to 31/03/2012 the expenditure has been debited under the head 'Bonus & Ex-gratia' and 'children education allowances'. The entries in the profit and loss account are not indicative to support the contention that these expenditure were incurred during 1999 to 2006, as no supporting information was filed to show that expenditure under the heads 'bonus and welfare expenditure' relate to these expenditure. Even assuming that the assessee had incurred these expenditure as claimed, they could have been incurred in his capacity as employer, as until 2004, the assessee was operating and manufacturing from Varalakshmi Jute Mill; and only the Vasavi Jute Mill was leased out in 1998. The assessee also filed payment details for the earlier years from 2007-08 onwards and also the FBT particulars relating to these payments. Further, the assessee also filed copy e-mail correspondence dated 08.02.2005, to the Chairman regarding proposal of

educational allowance to children of staff and workers of Vasavi Unit, which has been approved. Thus, on the basis of above material information on record it can be said that (a) there is clear evidence to show that there was a scheme for payment ex-gratia festival bonus and children education allowance since 2006, and it is not in dispute such claim has also been allowed by the department in the earlier years (b) the financial statements indicate payments of bonus and 'ex-gratia' prior to 2006 which may be in the capacity of employer (c) there is no clear evidence to show payment of educational allowance prior to 2005-06.

8.10. It was also contended that the lease of the factory was given along with the employees and that the assessee was under contractual obligation to make the impugned payments in furtherance of commitment made to the employees. I have perused the lease deeds

a) *between the assessee and Mahadev Jute & Twine Mills Pvt. Ltd. in regard to lease of Sri Vasavi Jute Mill vide agreement dated 06.11.1998.*
b) *the lease deed dated 215t August, 2004 between the assessee and M/s. Shree Vifayalakshmi Jute Mills in regard to lease of Varalakshmi Jute Mill with effect from September 2004.*
c) *the lease deed dated 07.10.2010 between the assessee and M/s.Nidhi Jute Mills in regard to lease of Vasavi Jute Mills.*

The lease agreements do not indicate any employer - employee relationship between the assessee and the workmen as pointed out by the AO. However, except the lease agreement dated 06.11.1998, the other lease deeds provide for continuity of services of the employees with the lessee.

Clause 18(a) of lease deed 21st August 2004 provide:

(i) *That the Lessee notwithstanding the transfer of establishment by way of lease will continue the service of all the employees of the Lessor whoever on the rolls of the Lessor company as on the date of transfer. In other words, former employees will have continuity of service on their accepting to continue their services with the Lessee firm after the transfer of Lease.*

a) *That the Lessee shall also be liable to continue the services of employees with the continuity of service benefits as it is and shall not modify them except under the due process of applicable laws.*
b) *The Lessee does not have any liability or responsibility in respect of employees whose services were terminated before the execution of lease deed.*

8.11 As per the Lease Agreement dated 07.06.2010 between the assessee as
Lessor and M/s. Nidhi Jute Mills in regard to Lease of Vasavi Jute Mill,

clause 15(i) provides that the Lessee undertakes that it shall continue to employ/ retain existing employees/ workmen of the lease unit in its pay roll and shall at all time ensure that the employees welfare and interest are taken care. The recital to the Lease Agreement also narrate that the Lessor has facilitated a joint meeting with the members and authorised representatives of Sri Vasati Jute Twine workers Union as to proposed change in the Lease and consequential change in the employment of the Union members working under present Lessee.

8.12 It is also relevant to note that the assessee retrenched employees of Sri Vasavi Jute Mill consequent to strike on 16.02.1998 with effect from 20.02.1998. Many of the retrenched employees were taken as employees by the then Lessee due to the intervention of the Collector. Thus the materials on record reveal (a) the employees of Vasavi Jute Mill (including some retrenched employees) and Varalakshmi Jute Mill who worked under the assessee, have continued to work with the Lessees of the mills after the execution of Lease (b) there was continuity of service of the employees with the Lessee (c) the Lessees have undertaken in the Lease Agreements to continue the services of the existing employees and ensure to take care their interest (d) the assessee had taken steps to ensure continuity of service of employees with the Lessees.

9. In the case of Tata Sons Ltd. vs. CIT (18 ITR 460) it was noted that the assessee, a managing agent company paid voluntarily half share of bonus which the managed company paid to its officers in order to increase efficiency of working of managed company which would result in higher and better profits of manufactured company and which tended to increase the income on profits of the assessee. The revenue objected to the allowability of the payment on the ground that the payment made was a voluntary payment and it was gratuitous in nature. However, the court found that the assessee company is directly and vitally interested in earning of the profits of the managed company and that there was sufficient commercial considerations for making the payment and hence can be allowed as a business deduction. The observation of the Hon'ble Bombay High Court Chief Justice Sri Chagla is relevant.

> *"I entirely and with very great respect agree with what their Lordships of the Privy Council stated, in the case of Tata Hydro-Electric Agencies vs. CIT (1937) 5 ITR 202 (PC). In that case their Lordships recognised, and decided cases show, how difficult it is to discriminate between expenditure which is and expenditure which is not solely expended and incurred for the purpose of earning profits or gains, but however difficult the task it has got to be attempted and we have to decide whether this particular deduction claimed by the assessee-company as a deduction is an expenditure laid out or expended wholly and exclusively for the purposes of the business of the assessee-company. Now, the decided cases show that one has not got to take an abstract or academic view of what is prover expenditure laid out or expended wholly and exclusively for the purposes of*

one's business. One has got to take into consideration questions of commercial expediency and the principles of ordinary commercial trading and the main consideration that has got to weigh with the Court is whether the expenditure was a part of the process of profit-making. If the expenditure helps or assists the assessee in making or increasing the profits, then undoubtedly that expenditure would be expended wholly and exclusively for the purposes of business. It has been urged by the Attorney-General that the payment made by the assessee was a voluntary payment. That is perfectly true, because there was no obligation whatever upon the assessee to share the bonus with the managed company, and in sharing the bonus the assessee did an act which it was under no obligation to do. But even a voluntary act if performed for commercial expediency would still be an expenditure falling within s. 10(2)(xv) if it can be shown that it was intended for the purpose of making or increasing the profits of the assessee-company. It has also been urged that the payment has been made not to the employees of the assessee-company but to the employees of the managed company, a different entity altogether. Here again if it can be shown that there was a very important nexus between the assessee-company and the managed company which necessitated the assessee-company making the payment to the employees of the managed company, then again it would be possible for the assessee-company to satisfy us that the expenditure was one which fell within the ambit of s. 10(2)(xv). Now it cannot be seriously disputed that the bonus was paid by the managed company to their employees in order to increase the efficiency of the working of the company. An increased efficiency of that company would incidentally result in higher and better profits, and the assessee-company would be as much interested in the working of the managed company being more efficient as the managed company itself. Whatever tended to increase the profits of the managed company would also tend to increase the income and profits of the assessee-company. Therefore it cannot be suggested that the assessee-company had an indirect or ulterior motive in making this payment.

It is also suggested by the Attorney-General that the payment by the assessee is entirely gratuitous and no consideration has been proved by the assessee for this payment. In my opinion the consideration is apparent on the face of the record before us. Once it is assumed, and I think we are justified in making that assumption, that the bonus was paid out of commercial considerations by the managed company, then in the payment of that bonus the assessee would be interested and when it shared that bonus it received part of the benefit which went to the managed company, and that part of the benefit would be the increased commission that the assessee would get by reason of the employees of the managed company being contented and having an impetus to work wholeheartedly and producing more profits for the employers.

3. Turning now to the cases that were cited at the Bar, in the

> *first place we have the judgment of Rankin, C.J., in the Anglo-Persian Oil Co. vs. CIT (1993) 1 ITR 129 (Cal.). In that case a lump sum was paid by an assessee as compensation for the loss of agency which was caused to its managing agents by the managing agency being terminated and instead of having to pay a recurring sum every year the assessee compounded its liability in a lump sum. The question that arose for the consideration of the Calcutta High Court was whether this payment was a permissible deduction. The two points which Sir George Rankin had to consider in his judgment were : (1) whether the payment was made solely for the purpose of earning profits, and (2) if so, the payment was made in the year of account. With regard to the first point the learned Chief Justice stated that if it appeared from the assessee's own case or the facts found that the payment was made by way of distribution of profits or was wholly gratuitous or for some improver or oblique purpose outside the course of business management, the deduction would not be permissible, but as no such suggestion had been made there was no reason why the deduction should be disallowed. In my opinion in the case before us also the payment is not wholly gratuitous nor is it for any improper or oblique purpose nor is it outside the course of the business management of the assessee-company.*

9.1 The Hon'ble Judge also referred to the decision of the House of Lords in Atherton's case (10 Tax cases 155), wherein Lord Viscount Cave made certain observations with regard to the nature of the expenditure which is wholly an expenditure laid out or expended for the purpose of trade which are very material. The same are referred in the decision as under:

> *It was made clear in the above cited cases... that 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". Therefore, it is quite clear that you may have a payment made voluntarily, you may have a payment made not for immediately benefiting the trade and which does not directly facilitate the carrying on of the business and yet the same can be said to have been expended wholly and exclusively for the purposes of the trade.*
>
> *But having considered the whole case and the question submitted to us I am satisfied that looking purely at it from the point of view of commercial principles what the assessee company has done is something which had as its object increasing the pro fits of the Tata Iron & Steel Co. and thereby increasing its own share of the commission. In that view of the case the only conclusion I can come to is that the sums claimed by the assessee-company were wholly and exclusively expended for the purposes of the business."*

9.2 The above observation of Lord Viscount Cave in the decision of

House of Lords in Atherton's case was referred by the Hon'ble Supreme Court in the case of CIT Vs. Chandulal Keshavlal & Co. (38 JR 601 SC). The facts in that case were that the assessee a managing agent foregone voluntarily part of the commission in favour of the managed company due to the unsatisfactory financial position of the managed company and claimed the same as business deduction. It was contended that the amount foregone by the managing agent had been given up in the interest of the managed company and therefore not an allowable deduction u/s.10(2)(xv). The court made the following observations and allowed the deduction.

> *"If the expense is incurred for fostering the business of another only or was made by way of distribution of profits or was wholly gratuitous or for some improper or oblique purpose outside the course of business then the expense is not deductible. In deciding whether a payment of money is a deductible expenditure one has to take into consideration questions of commercial expediency and the principles of ordinary commercial trading. If the payment or expenditure is incurred for the purpose of the trade of the assessee it does not matter that the payment may incur to the benefit of a third party : Usher's Wiltshire Brewery Ltd. vs. Bruce (supra). Another test is whether the transaction is properly entered into as a part of the assessee's legitimate commercial undertaking in order to facilitate the carrying on of its business; and it is immaterial that a third party also benefits thereby : Eastern Investments Ltd. vs. CIT (supra). But in every case it is a question of fact whether the expenditure was expended wholly and exclusively for the purpose of trade or business of the assessee. In the present case the finding is that it was laid out for the purpose of the assessee's business and there is evidence to support this finding. Mr. Palkhivala referred in this connection to Atherton vs. British Insulated & Helsby Cables Ltd. (1925) 10 Tax Cases 155 where at page 191 Viscount Cave L.C., observed:*
>
> > *"It was made clear in the above cited cases of Usher's Wiltshire Brewery vs. Bruce (supra) and Smith vs. Incorporated Council of Law Reporting (1914) 6 Tax Cases 477 that 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; and it appears to me that the findings of the Commissioners in the present case bring the payment in question within that description. They found (in words which I have already quoted) that the payment was made for the sound commercial purpose of enabling the company to retain the services of existing and future members of their staff and of increasing the efficiency of the staff; and after referring to the contention of the Crown that the sum*

> *of £31,784 was not money wholly and exclusively laid out for the purposes of the trade under the rule above referred to, they found that the deduction was admissible—thus in effect, although not in terms, negativing the Crown's contention. I think that there was ample material to support the findings of the Commissioners, and accordingly that this prohibition does not apply."*
> *Thus in cases like the present one in order to justify deduction the sum must be given up for reasons of commercial expediency; it may be voluntary, but so long as it is incurred for the assessee's benefit the deduction would be claimable.*

9.3 In the case of CiT vs. Raipur manufacturing company Ltd. (84 ITR 508, GUJ) the facts were the workers of the assessee company had formed cooperative society; where there was some mismanagement and misappropriation of the funds of the society and as a result, the society went into liquidation. The workers of the assessee company had put their savings in that society and suffered loss. As a result, there was unrest among the workers which was likely to adversely affect the business of the assessee. In the circumstances, the assessee company paid certain sum to liquidators of the society to make good the loss of the society. As such there was no legal obligation on the part of the assessee company to make such payment, but the court held that the amount is allowable as business expenditure on account of commercial expediency. It was contended that the said payment was made out of Generosity but was not a payment made of commercial expediency. The Court rejected the contention and observed….

> *"There was considerable discontent among the workers because of the loss of money to the society in which the workers had put in their savings. On several occasions there was tension and unrest in the factory premises and police had to be called to restore peace and order. It was apprehended that if the situation was allowed to continue for long, it might lead to strikes, stoppage of work and loss of lives of some of the officers of the company and neglect in work which may adversely affect the working of the company and thereby affect the quality and quantity of production. Against this background, the directors of the company considered the situation and passed a resolution to pay a sum of Rs. 76,161 to the liquidator of the society to make good the loss. The resolution noted that the amount was being paid in order to maintain peace and good relations with the employees of the company. If in order to avoid adverse consequences which might lead to loss to the assessee company, the assessee company decided to purchase peace so that the company could go on with its production by securing the co- operation of the workers and the company*

decided to make the payment in question, it could not be said that the payment was not made out of the commercial expediency. Though the assessee was not bound to make the payment, the nexus between the payment and the commercial expediency was very clear, i.e., the smooth working of the factory being ensured and the unrest among the employees eliminated to a certain extent. Under these circumstances, the Tribunal was right in coming to the conclusion that the expenditure in question was laid out wholly and exclusively for the purposes of the assessee-company's business."

9.4 The court also referred the decision in the case of 3. R. Patel & Sons (P.) Ltd. vs. CIT (69 ITR 782 Guj.) wherein it was held that the correct approach would be to see whether the payment was made on grounds of commercial expediency for the ultimate business of the assessee, whether that benefit is accrued immediately or after a lapse of time and whether directly or indirectly immaterial. The court observed:

"(1) One has not got to take an abstract or academic view of what was proper expenditure laid out or expended wholly and exclusively for the purposes of one's business but one has got to take into consideration questions of commercial expediency and the principles of ordinary commercial trading and the main consideration that has got to weigh with the Court is whether the expenditure was a part of the process of profit making.

The test for the purpose of deciding whether a particular amount can be allowed as deductible allowance under s. 12(2) of the Act is whether the transaction is properly entered into as a part of the assessee's legitimate commercial undertakings in order indirectly to facilitate the carrying on of its business. If the transaction had been entered into on the ground of commercial expediency in order even indirectly to facilitate the carrying on of the business of the assessee, it would attract the provisions of s. 12(2) even though the transaction might have been voluntarily entered into.

If the payment was made with an indirect or improper motive for some considerations aliunde the business or out of generosity, then the payment is not liable to be regarded as one covered by the provisions of s. 10(2)(xv) that the matter has to be viewed in the light of principles of commercial trading and commercial expediency and what is required is that the expenditure must be germane to the business of the assessee and not something which is de hors the business."

9.5 In the case of CIT v Tata Sons Ltd. (111 ITR 290) the facts were that the assessee company was acting as a managing agent of one Ahmedabad Advance Mills. On the operation of the golden jubilee celebrations of the connection mills the assessee company contributed Rs. 1 lakh to management. The amount was given to the mills without being earmarked for any particular business and that amount was utilized by the managed mills for construction of canteen for its workers. The assessee company claimed the amount as permissible deduction which was rejected by the ITO. The Hon'ble court following the decision of Supreme Court in the case of CIT vs. Chandulal Keshavalal & Co. held that the deduction is allowable.

9.6 In the case of CIT vs. Sales Magnesite Pvt. Ltd. (214 ITR 1) the facts before the Bombay High Court was that the assessee company terminated the sole selling agency held by the agent for 3 decades for which the agent claimed certain compensation. The assessee company paid compensation and claimed the same as deduction. The court found that the assessee was not bound to pay compensation but even then it can be claimed as business deduction as the said expenditure was incurred on the basis of business considerations, and as the compensation paid was not illusory or malafide.

9.7 In the case of CIT vs.. Dhanrajgirji Raja Narsingingi (91 1TR 594 SC) the facts before the Supreme Court was that the assessee incurred certain expenditure in connection with criminal litigation. The department did not allow the expenditure on the ground that the Government was conducting the prosecution and that there was no necessity for the assessee to incur the expenditure. The court rejected the contention and held that it was for the assessee to decide how best to protect its own interest. It is not open to the department to prescribe what expenditure should assessee incur and in what circumstances the assessee incur such expenditure. Every business man knows his interest best.

9.8 In the case of CIT vs Gobald Motor Services Pvt. Ltd. the Hon'ble Madras High Court observed:

> *It should also be borne in mind that the jurisdiction of the revenue in this regard is confined to deciding the reality of the expenditure and whether it was wholly or excessively for the purpose of the business and it is not for the revenue to question the commercial expediency of the expenditure. Commercial expediency is a matter entirely left to the judgment of the assessee."*

9.9 In the case of CIT vs. Associated Electrical Agency (226 1TR 63) the Hon'ble Madras High Court observed that:

> *'Payments made having regard to the commercial expediency, need not necessarily have their origin in contractual obligations. If an assessee, who carries on a business finds that it is commercially expedient to incur*

certain expenditure directly or indirectly, it would be open to such an assessee to do so notwithstanding the fact that a formal deed does not precede the incurring of such expenditure.

Judicial opinion is, however, unanimous to be extent that there is no single test which can be said to be universal application nor is there a test which would hold good in every conceivable situation. The situational diversities are in fact so innumerable that even the Parliament has in its supreme wisdom avoided to give any precise definition to the expressions. Courts have, therefore, been extremely cautious in formulating any general principles candidly recognizing that it is difficult to formulate a test or principle which may be sufficiently accurate and yet exhaustive enough to cover all possible cases.

9.10 In the case of CIT vs. Delhi Safe Deposit Co. Ltd. 133 ITR 756 (SC) held that

"The true test of an expenditure laid out wholly and exclusively for the purposes of trade or business is that it is incurred by the assessee as incident to his trade for the purpose of keeping the trade going and of making it pay and not in any other capacity than of a trader. The assessee incurred the impugned expenditure to avoid any adverse effect on its reputation to protect the managing agency which was an income earning apparatus and for retaining it with the reconstituted firm in which the interest of the assessee was the same as before. It was likely that but for the expenditure, the fair name of the assessee would have been tarnished or rendered suspicious and the managing agency would have been terminated. The expenditure incurred on the preservation of a profit earning asset of a business has always been held to be a deductible expenditure by the courts. In the circumstances, it was difficult to hold that the expenditure incurred by the assessee as either gratuitous or one incurred outside the trading activities of the assessee. The expenditure was therefore deductible under section 37(1).

9.11 The Hon'ble Supreme Court in the case of Gordon Woodroffe Leather Manufacturing Co. (44 ITR 551) laid down the following tests on allowability of gratuity payments as business deduction:

Was the payment made as a matter of practice which effected the quantum of salary or was there an expectation by the employee of getting 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.

9.12 If any of the above tests were satisfied, the payment of gratuity or

pension were held to be allowable as deduction, as could be seen from the

decisions of A.P. High Court in the case of British India Tobocco Corporation Ltd. (79 ITR 41 AP), Madras High Court in the case of Lucas Indian Services Ltd. 239 ITR 429 and CIT vs. Laxmi Cement Distributors Pvt. Ltd. (104 ITR 711 GUI) and other cases. Few other decisions are discussed at para (13) of the order.

9*.13 Considering the principles laid down in above judicial decisions it can be said that payments/ expenditure incurred voluntarily out of business consideration is allowable even if there is no legal compulsion to make the payments; provided the said expenditure was incurred as part of the process of profit making. Even an expenditure incurred which indirectly facilitate the carrying on of the business is allowable as one of business expediency. If the payment was made out of business expediency it cannot be said to be wholly gratuitous. The nexus between the payment and commercial expediency has to be clear. Expenditure in the nature of pension, gratuity are allowable if any of tests laid down by the apex court in the case of Gordon Woodroff Leather Manufacturing Co. are satisfied.*

9.14 The factual conspectus of the present case would reveal that the assessee company ceased to be the employer with the leasing of the units. As per the Board resolutions the impugned payments were made for smooth operating of the lease and to improve the morality and efficiency of the workers even though the units have been leased. Thus it is quite implicit that the impugned payments are not made out of strict legal obligation. The payments have been made as per policy of the company and as per scheme adopted; and there is clear evidence to show that the payments have been made in the last 5 or 6 years. It was contended that the payments were made as part of contractual obligation. But the assessee could not produce any written agreement or arrangement entered with the workers or with the lessee for such contractual obligation. However, from the scheme which is put in place for making these payments it could be inferred that the assessee has assumed this obligation; the fact that these payments have been made consistently for the past five or six years would clearly show that the employees would definitely formed a reasonable expectation that these payments would be paid for the subject year also.

9.15 The most important question to be addressed is whether the impugned payments are made out of business considerations and out of commercial expediency. The assessee company leased out the two mills which effectively mean that the Lessee would be in possession of the factory premises and also operate and manage the mills. As per the Lease Agreement, the Lessee is required to refer in all its letter pad, name plates and correspondence explicitly, "Lessees of" Vasavi unit and currently under Lease from Sri Varalakshmi Jute Twine Mills Pvt. Ltd. The lease deed dated 07.06.20 10 provides that if there is a delay in payment of lease rent for more than 2 months, and the payment not made in 15 days notice, then that amount to 'breach'; and the Lessor would be entitled to terminate the lease without any notice. The Lease can also be terminated by giving 4 months prior notice. The regular payment of lease rent

would depend on the revenue generated and the smooth functioning of the units which no doubt requires the cooperation and support of the labour. Thus, the assessee company cannot afford to remain oblivious to the employees' interest to see that the employees work efficiently and without creating any unrest or labour problems. It is evident that the assessee has direct interest in the smooth operation of lease. The lease deeds also reveal that the assessee company has facilitated meeting with the Employees Union to facilitate smooth transition of lease from one Lessee to another. The Lease deeds also provide that the Lessees undertake to ensure continuity of service of the employees without affecting their terms of service and also to take care of their interests. Therefore, the payments made by the assessee company towards the employees welfare can be said to be out of its own business interests and out of commercial expediency. There is a clear nexus between the impugned payments and the assessee's business interests. The impugned payments were not illusory and were not made for improper or oblique purpose outside the course of business. Besides, it is also noted that the impugned payments were made under a scheme and consistently for the past 5 or 6 years. The employees reasonably expect such payment in this year also. The assessee has clarified that these welfare payments are not borne by the Lessee under the Lease. The nature of payments are such that it would improve the efficiency of the workers and their commitment. These welfare payments are not unusual in this line of industry. I find that the ratio laid down by justice Chagla in Tata Sons Ltd. vs. CiT (18 ITR 460) and the principle laid down by the Hon'ble apex court in the case of Chandulal Keshavlal & Co. are clearly applicable. The assesse also satisfies the tests laid down in Gordon Woodroffe case by the apex court. Therefore, it is held that thei impugned payments in the nature of ex-gratia festival bonus and children education allowance are allowable as business deduction as they are made as part of a scheme and were incurred out of commercial expediency.

9.16 The assessee has shown payment of Rs.31,58,852/- towards children education allowance. The verification of the details filed show that the following payments

04.06.2011	Rs.	65,000/-
27.06.2011	Rs.	*9,190/-*
12.07.2011	Rs.	9,000/-
28.09.2011	Rs.	14,750/-
30.11.2011	Rs.	*25,000/-*
Total	Rs.	1,22,940/-

are not made under the scheme and the assessee has not proved the business expediency in making these payments. Therefore the Assessing Officer is directed to restrict the disallowance to Rs. 1,22,940/- out of Rs. 31,58,852/- in regard to children education allowance. With regard to ex-gratia bonus, it is

noted that payment of Rs. 4,500/- on 18/01/2012 was not under the scheme and the business expediency of the same was not proved. The same may be disallowed. The balance amount paid towards festival ex-gratia allowance may be allowed."

9. On being aggrieved, revenue carried the matter in appeal before the Tribunal.

10. Ld. Departmental Representative has submitted that the assessee has incurred certain expenditure i.e. children education and bonus without there being any statutory obligation on the part of the assessee to make such payments. There is no employer and employee relationship between them. Therefore, the expenditure incurred by the assessee cannot be allowed. He further submitted that the expenditure incurred by the assessee cannot be covered under section 37 of the Act and submitted that order passed by the ld. CIT(A) may be reversed to the extent of relief granted to the assessee.

11. On the other hand, ld. counsel for the assessee has submitted that payments made by the assessee to the ex-employees as per prior agreement i.e. before the date of leasing out factory to the lessee. Therefore, it is a commitment made by the assessee to the ex-employees and according to the commitment, the assessee has paid the amounts, therefore, the

same has to be allowed even though there is no contractual obligation on the part of the assessee to pay the same.

12. He further submitted that assessee is in the business of running a jute mills and it is labour oriented business to run the industries smoothly though the factories are leased-out, it is ultimate necessity of the assessee to see that the business has to run smoothly. Therefore, the payments made by the assessee are for business purpose, hence, allowable under section 37 of the Act.

13. We have heard both the sides, perused the material available on record and orders of the authorities below.

14. The assessee – M/s. Sri Varalakshmi Jute Twine Mills Pvt. Ltd. incurred certain expenditure towards children education and bonus. The case of the Assessing Officer is that the assessee has incurred the above expenditure without any contractual liability to make the impugned payments and there is no employer and employee relationship, therefore it cannot be allowed. The case of the assessee is that the payments made by the assessee to the ex-employees, is a prior commitment before the date of leasing out factory to the lessee. Therefore, even if there is no contractual obligation, to run the business smoothly, the

payments have been made hence, the same has to be allowed under section 37 of the Act.

15. We have gone through the orders passed by the Assessing Officer as well as ld. CIT(A). The ld. CIT(A) after considering the relevant material placed, he gave a categorical finding in his order at page No. 33 that there is a clear evidence to show that there was a scheme for payment of *exgratia,* festival bonus and children education allowance since 2006 and it is not in dispute such claim has also been allowed by the department in the earlier years; the financial statements indicate payments of bonus and *exgratia* prior to 2006 which may be in the capacity of employer; there is no clear evidence to show about the payment of educational allowance prior to 2005-06. The ld. CIT(A) gave further finding that factual conspectus of the present case would reveal that the assessee company ceased to be the employer with the leasing of the units. As per the Board resolutions, the impugned payments were made for smooth operating of the lease and to improve the morality and efficiency of the workers, even though the units have been leased. Thus, it is quite implicit that the impugned payments are not made out of strict legal obligation. The payments have been made as per policy of the company and as per scheme

adopted; there is a clear evidence to show that the payments have been made in the last 5 or 6 years. The assessee is paying continuously to the employees and therefore it could be inferred that the assessee has assumed this obligation, and also the fact that these payments have been made consistently for the past five or six years would clearly show that the employees would definitely formed a reasonable expectation that these payments would be paid for the subject year also. From the above finding of the ld. CIT(A), it is clear that before leasing out the factory, the assessee has been paying the above payments continuously to the employees and therefore the assessee has paid the same in year under consideration as a reasonable expectation from the workmen and accordingly payments are made. By considering the facts and circumstances of the case, though strictly these payments are not according to the contractual obligation, take into consideration of the nature of the business and also the payments are made even in earlier years, therefore, the payments made by the assessee is justified on the ground of reasonable expectation from the employees of the company.

16. So far as business expediency is concerned, the ld. CIT(A) by relying on the decisions of the Apex Court in the case of *CIT vs.*

Chandulal Keshavalal & Co. (38 ITR 601); *CIT vs. Tata Sons Ltd*. (111 ITR 290) and also *Gordon Woodroffe Leather Manufacturing Co.* (44 ITR 551) observed that assessee-company has leased out the two mills which effectively mean that the lessee would be in possession of the factory premises and also operate and manage the mills. As per the lease agreement, the lessee is required to refer in all its letter pad, name plates and correspondence explicitly, 'lessees of' Vasavi Unit and currently under lease from Sri Varalakshmi Jute Twine Mills Pvt. Ltd. The lease deed dated 07/06/2010 provides that if there is a delay in payment of lease rent for more than 2 months, and the payment not made in 15 days notice, then that amounts to 'breach' and the lesser would be entitled to terminate the lease without any notice. The lease can also be terminated by giving 4 months prior notice. The regular payment of lease rent would depend on the revenue generated and the smooth functioning of the units, which no doubt requires cooperation and support of the labour. Thus, the assessee company cannot afford to remain oblivious to the employees' interest or the issues faced by the employees. It is in the assessee's business interest to see that the employees work efficiently and without creating any unrest or labour problems. It

is evident that the assessee has direct interest in smooth operation of lease. The lease deeds also reveal that the assessee company has facilitated meeting with the employees union to facilitate smooth transaction of lease from one lessee to another. The lease deeds also provide that the lessees undertake to ensure continuity of service of the employees without affecting their terms of service and also to take care of their interest. Therefore, the payments made by the assessee company towards the employees' welfare can be said to be out of its own business interest and out of commercial expediency. There is a clear nexus between the impugned payments and the assessee's business interests. Therefore, the impugned payments are in the nature of exgratia, festival bonus and children education are allowable as business deduction as they are made as part of a scheme and were incurred out of commercial expediency.

17. From the above categorical finding of the ld. CIT(A), it is very clear that there is a proximity between the assessee company and the employees, and the payments made for the business interest of the assessee. Take into consideration of the nature of the business carried out by the assessee and facts and circumstances prevailing in the industry, in which the assessee is

carrying business and also by considering the past experience with the employees, we find that the assessee has paid these payments out of business interest and therefore allowable under section 37 of the Act. We also find that ld. CIT(A) has passed a detailed order by following the decisions of the Hon'ble Supreme Court in the cases *Tata Sons Ltd.* (supra) and also *Gordon Woodroffe Leather Manufacturing Co.* (supra) and hold that the expenses incurred by the assessee are out of commercial expediency, therefore, we find no infirmity in the order passed by the ld. CIT(A). The assessee has shown payments of Rs.31,58,852/- towards Children Education Allowance. The ld.CIT(A), after verifying the details, found that for the amount of Rs. 1,22,940/- assessee has not proved the business expediency, therefore, he has directed the Assessing Officer to restrict the disallowance to Rs. 1,22,940/-, out of Rs. 31,58,852/-. With regard to *exgratia* bonus, it is found that payment of Rs.4,05,000/- is not according to the scheme and there is no business expediency, therefore, the same is disallowed from the festival bonus.

18. So far as other expenses claimed by the assessee are concerned, the ld. CIT(A) in his order at page No. 43 has

examined the details and held that the amounts paid to nine employees are not proved that these payments have been made in pursuance of the scheme and were out of business expediency. Assessee has filed payment particulars without any supportive evidence to show that these expenditure was incurred for the purposes stated and in relating to the ex-employees presently working in the leased units. Therefore, the ld. CIT(A) has confirmed the order of the Assessing Officer insofar as payments made to 9 employees. The details of the payments made, are as under:-

Sl.No.	Particulars	Amount (Rs.)	Purpose of payment explained to AO during assessment proceedings	Remarks
1	Amount paid to Mr. Appa Rao for expenses on Medical treatment	48,000	The said payment represents payment made for the expenses on medical treatment of Mr Appa Rao, a former worker of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company. The proof of payment made is attached herewith in Annexure-III	
2	Amount paid to G. Bhushana Rao for medical treatment	4,800	The said payment represents payment made for the expenses on medical treatment of Mr.G.Bhushana Rao, a former workmen of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company. The proof of payment made is attached	

			herewith in Annexure-IV	
3	Payment of Medical Insurance for the workers of Varalakshmi Unit	17,626	The said payment represents payment made for medical insurance to United India Insurance company for carrying out group medi-claim for the workmen of Sri Varalakshmi Jute Mills which have been leased Out to M/s Howarh Mills Company Limited. The copy of insurance policy in support of making payment for the medical insurance for the workmen of Sri Varalakshmi Jute Mills is attached herewith in Annexure-V	
4	Expenses paid to SV Diwakara Rao, ex-employee, for expenses on Medical treatment	35,000	The said payment represents payment made for the expenses on medical treatment of Mr S.V. Diwakara Rao, a former workmen of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company. The proof of payment made is attached herewith in Annexure-VI	
5	Amount paid to B. Maralidhar (for daughter's marriage)	5,000	The said payment represents payment made at the occasion of daughter marriage of Mr B. Muralidhar a former associate of Sri Varalakshmi Jute Mills.	
6	Amount paid to B. Ramesh Babu for expenses on Medical treatment	48,000	The said payment represents payment made for the expenses on medical treatment extended by Dr. B. Ramesh to the workers/ staff of the Company presently working with the Sri Vasavi Jute Mills which has been leased out to M/s. Nidhi Jute Mills by the assessee company. The proof of payment made is attached herewith in Annexure-VII	
7	Ex-gratia function expenses	79,540	These expenses were incurred for the lumpsum Ex-gratia distribution function held on 13-01-2012 an the	

			details of expenses under various heads such as snacks, tea, coffee, rent for chairs, pendal, photograph expenses etc. and the details are furnished in Annexure-IX	
8	Varalakshmi Jute Mills workers children education	8,500	The said payment represents payment made towards expenses on education of former workmen which a currently working with Sri Varalakshmi Jute mills lease out to by the assessee company to M/s. Howarh Mills Company Limited. The proof of payment made is attached herewith in Annexure-X	
9	Payment made to Mr.Surabhi Satish, an ex-worker to support expenses on the marriage of her dependent-sister	1,00,000	The said payment represents payment made to Surabhi Satish, a Former associate of the Company. Financial help is extended by the company against the representation received from the associate. The proof of payment made is attached herewith in Annexure-XI	
10	Other staff welfare expenses	64,006	The complete details of other welfare expenses is enclosed herewith in Annexure-XVI.	

19. So far as payment made to Sri T. Sangam ex-employee of Rs. 15,000/-. The assessee has submitted before the ld. CIT(A) that the disallowance has been made twice, therefore, the Assessing Officer is directed to verify and allow the same, if such contention is found to be correct. We find no infirmity in the order passed by the ld. CIT(A).

20. With regard to payments made to Arya Vysya Yuva Jana Sang dated 08/07/2011 of Rs. 1,50,000/- and payments made to S. Nanaji of Rs. 1,50,000/-, it was submitted before the ld. CIT(A)

that the above amounts are advances made to these parties and not expenditure incurred by the assessee, but were debited to the profit & loss account. Therefore, ld. CIT(A) directed the Assessing Officer to examine the claim and allow, if it is found that these expenditure were debited to the profit & loss account.

21. So far as *exgratia* function expenses of Rs. 79,540/- are concerned, it was submitted before the ld. CIT(A) that it is incurred for the purpose of lumpsum *exgratia* distribution function held on 13/01/2012 and also submitted that these expenses were to boost the morale of the employees. The ld. CIT(A) found that the above expenses are incurred for the purpose of business expediency and directed the Assessing Officer to allow the same. We find no infirmity in the order passed by the ld. CIT(A).

22. Insofar as lump sum exgratia payment of Rs. 97,47,042/- is concerned, the Assessing Officer has noted in the assessment order that after examining the books of account and other relevant facts, the expenditure incurred by the assessee cannot be allowed for the reason that there is no employer and employee relationship among them and assessee also could not produce any documentary evidence to prove that the subject expenditure is a

statutory liability / necessity, it would be paid to the employees and lump sum exgratia made by the assessee was disallowed.

23. On appeal, it was submitted before the ld. CIT(A) that on the basis of contractual obligation with reference to commitment made by the management to reward the employees for their long services and continuity of their service with different lessees and extending their support during difficult days. It is also submitted that to maintain good relationship with the workers and as there is continues labour problem and there is a difficult to get skilled workers. It is also submitted that to fulfil the expectations of the employees arising out of the commitment given by the management, to avoid labour unrest and ensure industrial peace in the business interest of the assessee. It is also submitted that it is a commercial expediency of the assessee and also to safeguard to legitimate business needs of the assessee company. The ld. CIT(A) after considering the above explanation and also details filed by the assessee, passed a detailed order. The relevant portion of the order is extracted as under:-

> *"11.15 As per the resolution from the minutes of the Board meeting held on 4th December 2011, it was mentioned that the chairman informed the Board that, a commitment was made to its ex-workers and staff to provide some financial support as gratitude towards their continuous services rendered and co-operation extended during the critical situations of the company the Board*

members discussed and agreed to pay a lump sum of Rs.2 crores approximately towards ex-gratia payment to the ex-workers and staff proportionate to the services rendered by them in company and with the lessee. The letter dated 24.08.2011 from Mills. Nidhi Mills stated that it was given to understand from the workmen from time to time, who were working with the assessee company ad continued with the lessee company that the assessee management promised to give ex-gratia payment in course of time, and it was reminded that the promise was not fulfilled the date. It further stated that the workmen threatened to stop the work till the time their ex-gratia payment was settled, and hence it was suggested to the assessee to settle the issue for continuous and smooth operation of the mill which will be advantageous to both. The payment details were filed along with the bank statement.

11.16 Annexure-VII to the letter dated 27.03.2015 submitted to the Assessing Officer contain proposal regarding the lumpsurn ex-gratia payment according to which the following categories of workmen were considered for the lumpsum exgratia allowance.

a) INTUC Ex-*Vasavi workers presently working in Nidhi*.
b) INTUC Ex-*Vasavi workers working outside.*
c) CITU Ex-Vasavi workers working in Nidhi.
d) CITU Ex-Vasavi workers working outside (Not recommended)
e) Staff.

11.17 A few letters from the employees requesting for some financial assistance were also filed. These letters refer to the financial assistance assured by the Chairman at the time of strike and as to the commitment of the workers in working with same spirit and zeal for several years (P.179 - 193 of FPB).

11.18 As per payment details, it is seen that 334 employees were paid total amount of Rs.97,47,082/- through cheque. The assessee was requested to furnish details of joining and exit from employment for all these workmen. From the details filed, it is seen that 83 workers were on rolls only up to 16.02.1998 and ex-gratia lumpsum payment have been paid to them and which amounted to Rs.12,29,167/-.

11.19 The common award passed by the Industrial Tribunal Cum Labour Court, Visakhapatnam vide order in I.D. No.243/1998 & I.D.No.181/1999 dated 09.07.2009 was perused. It is seen that the General Secretary of M/s. Rajam Jut Mills Workers Union and M/s. Sri Vasavi Jute and Twine Workers Union have preferred the claim against the management of M/s.Sri Vasavi Jute and Twine Mills Pvt. Ltd. In the award, it is discussed that the first claimant Rajam Jute Mills Workers Union was affiliated to C.I.T.U. whereas the second claimant Sri Vasavi Jute Twine Workers Union was

affiliated to I.N.T.U.C. The award records that the second union has not raised any dispute or laying any claim over the management and was also supporting the management. The first claimant is the author of the dispute. It was further noted that the first union came into existence in the year 1996. Earlier there were several agreements between the second union representing the workmen and the management. Disputes cropped up when the representation of certain workers represented by the first union presented a charter of demands on 21.06.1997 which were not acceptable by the management. As a result there was a lightning strike from 16.02.1998. As the situation went out of control creating unrest in the premises police were deployed on 19.10.1998 and prohibitory orders were also promulgated. Ultimately the management had claimed lock-out of the factory with effect from 20.02.1998. It is also recorded that the management had retrenched the services of 220 workmen belonging to the first union by paying the compensation. During the pendency of conciliation proceedings before the Dy. Commissioner (Labour), the management had transferred the factory by way of lease on 06.11.1998 to Mahadev Jute Mills. The above award has been challenged before the A.P. High Court and is pending.

12. It is seen that the Hon'be Supreme Court in the case of Gordon Woodroffe Leather Mfg. Co- vs. CIT (44 ITR 551) laid dawn the following test:

> *a) Was the payment made as a matter of practice which affected the quantum of salary, or was there an expectation by the employees of getting the 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.*

12.1 In the case of British India Tobacco Corporation Ltd. vs. CIT, the issue before the Hon'ble Andhra Pradesh High Court was whether the payment of a sum of Rs.88,000/- towards pension to the Director of the company as his retirement would be a permissible deduction. The court held that the amount is allowable as deduction as there was commercial expediency and there was an expectation on the part of the employees in getting the said sum. The court also opined that the tests laid down by the Supreme Court are alternative test. The court observed:

> *"On the facts of this case; it was clear that the payment made to the Life Insurance Corporation was made 'on the ground of commercial expediency and in order indirectly to facilitate the carrying on the business of the Corporation and there was also an expectation on the part of the employee petting the said sum. These two*

requirements were fully satisfied, for fl, when he was due to retire in 1957, agreed to continue in service only in expectation of the payment of the pension for a period of ten years and the company likewise did not intend to pay him gratuitously in view of his past services but agreed to pay the pension with a view to secure his services for a further period of three years. By no stretch of imagination could this payment be treated as a gratuitous payment to AT'. In the decision relied upon for the revenue, the payment that was made was not pension was gratuity. That apart, the decision to make that payment was taken on the expiration of the term of service, In fact it was decided upon after the employees resignation was accepted.

The other test, viz., that the payment should have been made as a matter of practice, was applied In those circumstances The Supreme Court, did not intend to lay down that any payment made contrary to the practice prevailing as the payment of pension or gratuity should necessarily be held to be an inadmissible deduction. In court's opinion, what the Supreme Court Intended to lay down was that if there was such a practice it would go a long way to satisfy the main test laid down by the Supreme Court, viz., that it was not a gratuitous payment and that it was a payment on the ground of commercial expediency to facilitate the carrying on of the business. It was clear from the judgment of the Supreme Court that these were two alternative tests that could be applied to determine whether such a payment could be held to be a permissible deduction. In the instant case, in our view, the resolutions recorded on 19-12-1957, varied the terms of the service agreement of the assessee-company with 'AT'. As a result of the above, 'N had an expectation of getting the pension and the company had incurred that liability on the ground of commercial expediency to indirectly facilitate the carrying on of its business. It was only in discharge of that liability that the subsequent two resolutions were adopted after his retirement and the payment of Ps. 8$1000 was made to the Life Insurance Corporation for securing the payment of pension to 'AT'. This deduction was clearly a permissible deduction in the computation of the assessee's business income

12.2 In the case of CIT vs. Sinnar Bidi Udyag, the brief facts were that the assessee was a Bidi manufacturer company took over the affairs at the earlier company and services of employees

are continued. The assessee claimed deduction of an amount of Rs.3.71 lacks an account of retirement compensation paid to several workers an retirement, and which related to services rendered by the employees for the prior period. The issue was whether the payment made for the earlier period would be an allowable deduction. The court held that the affairs of the earlier company was taken over by the assessee company and the services were continuous, and as a result the workers had legitimate expectation that their service will also be considered for calculating the gratuity. The court made the following observation:

> *"Although the payment was made for the services rendered by the employees concerned for the period prior to their joining into the assessee-company, the assessee-company had considered their representation and thereafter, settled the matter with the employees. The assessee-company had considered the fact that the affairs of the earlier company were taken over by the assessee-company and the services of the employees were continuous and they had put in long valuable service over the years. Since the affairs of the earlier company were taken over and the services were continuous, the workers had legitimate expectation that their earlier service will also be considered for calculating gratuity. The employees had also initiated proceedings against the respondent-company first before the Labour Commissioner and thereafter before the gratuity authority. It was thereafter that the necessary decision was taken by the respondent-company to settle the controversy. The respondent-company accepted part of the claim by passing a resolution in the meeting of board of directors. Therefore, it was to be held that this payment had been made to the employees by way of commercial expediency also.*
>
> *It was not a payment either towards or from the gratuity fund. It was a payment in excess of the payment that would be required to be made under the Payment of Gratuity Act, though made on the basis of legitimate expectations of the workmen in the facts of the case on the one hand and the commercial expediency of the employer on the other.*
>
> *It is well settled that the legitimate business needs of an assessee must be judged from the point of view of business. It is for the assessee to consider the business expediency and whether a provision of gratuity to the employees for the continuous services rendered to the company taken over could not be said to be either*

unusual or unnecessary. The workmen had come to expect such provision or their legitimate due and in the instant case they had in fact filed application before the payment of Gratuity Authority. The resolution of the board of directors also accepted their legitimate dues.

In the circumstances, the deduction claimed by the company would not fall under section 36(1)(v), but would be in the nature of revenue expenditure wholly and exclusively for the purposes of business. In that view of the matter, the decision arrived at by the Commissioner (Appeals) as well as by the Tribunal could not be faulted and the Tribunal was justified in coming to the conclusion in the facts and circumstances of the case that the expenditure of Rs. 3.70 lakhs incurred by the assessee as retirement compensation was allowable as revenue expenditure.

12.3 In the case of CIT vs. Shaw Wallace & Co. Ltd. the issue before the Hon'ble Calcutta High Court was whether exgratia payment made to workers in terms of development to keep good relation with workers in excess of limitation provided under payment of Bonus Act would be an allowable expenditure. The court took the view that the additional amount in the form of exgratia payment made by the company to the labourers and staff was expended wholly and exclusively for the purpose of business to keep the labourers satisfied and to buy industrial peace and to avoid strikes and lockouts; and therefore such expenditure paid in excess of bonus in the nature of exgratia payment would be allowable as business expenditure u/s.37. The court relied on the following decisions of the Hon'ble Madras High Court (a) CIT vs D Mohammed Ismail (227 ITR 211) wherein the Hon'ble Madras High Court held that the customary bonus paid to the employees as a matter of fact satisfied the conditions prescribed under the 2nd proviso to section 36(1)(4). (b) CIT vs. Tyagarajar Mills Ltd. 237 FIR 857 wherein it was held that incentive bonus is an allowable deduction u/s.37 of the I T Act. (c) Kumaran Mills vs. CIT (241 FIR 564) wherein it was held that the payment made over and above the statutory maximum to the labourers pursuant to an agreement under the Industrial Dispute Act was deductible u/s.37 and held that such payment would be for the purpose of commercial expediency and allowable u/s.37 of the I T Act.

12.4 In the case of ITO vs. Taj Services P. Ltd. (24 taxmann.com 83) the Hon'ble Mumbal FIAT he'd that the payment made to the workmen engaged by contractors to settle disputes on account of which the assessee derived an apparent advantage in the form of reduced car hire charges and as it benefits the business, the

deduction allowable u/s.37 of the I.T.Act.

13. The following decisions rendered by the various High Courts in regard to allowability of 'pension' or 'gratuity' in the light of tests laid down by the Hon'ble Supreme Court are relevant for consideration:

1) *In the case of Teekoy Rubbers (India) Ltd. vs. State of Kerala (60 ITR 350). the Kerala High Court held that the payment of gratuity to the widow of an ex-employee could not be allowable as the nexus between the payment and the future conduct of the business was found lacking. Similar view was taken in the case of) & K woolen Manufacturers Ltd. vs. CIT(46 ITR 123 (All.) & Lakshmichand Mucchal vs CIT (48 ITR 560 MP).*
2) *In the case of Airways (India) Ltd. vs. CIT the Calcutta High Court held that the compensation paid on premature termination of managing agency in the case of virtual closure of business would not be an allowable deduction. The court opined that the expression for the purpose of business' could only mean something which could further the cause of the business; something which would aid in the carrying on the business or prolong effectively the life of the company. If the business itself were coming to an end then the compensation paid to the managing agent would not fall within the purview of section 10(2)(xv).*
3) *In the case of Indian Overseas Bank Ltd. vs. CIT (63 ITR 733), the Madras High Court held that pension paid to an employee pursuant to Board resolution would be an allowable deduction though there was no general scheme for payment of pension as the expenditure was found to be made in the interest of assessee's business as the employee would not accept any other banking employment. The court opined that though there might not pension scheme, still in exceptional cases businessman could enter into contract of service providing for pension and claim deduction of pension paid. The first question to keep in view was whether the expenditure claimed was laid out for the purpose of business, whether it was a legitimate business expenditure and whether it was in the interest of the business. The directorate of the business itself was the best judge in the matter, for it was for them to consider the business expediency and whether a particular expenditure was incurred for the purpose of the business.*
4) *In the case of Dholpur Glass Works Ltd. vs. CIT (72 ITR 278), the court held that the payment made to managing agents in addition to commission on profits was only to secure the goodwill of the managing agents and not for the purpose of promoting the business of the assessee company. Amount paid for past services and past sacrifices*

will not be a business expenditure.

5) *In the case of W.T. Suren & Co. (P) Ltd vs. CIT (80 ITR 602), the pension payment made to two of the old employees of the company was found primarily in consideration of past services rendered by them to the firm the business of which was taken over by the assessee Limited Company. The court found that the payment cannot be inferred to have been made to safeguard the company against competition by these servants.*

6) *In the case of Seshasayee Bros. Pvt. Ltd. vs. CIT (82 ITR 442), it was seen that the company has made payment of pension to widow of the deceased director, the court found that the director was not an employee of the company, the payment of pension was not covered by any scheme, arrangement, and that there was nothing to show that there was any expectation in the mind of the director that pension would be paid to him or his widow. Therefore, the pension paid to the widow was held to be not deductible.*

7) *In the case of Commissioner of Agricultural Income Tax vs. Craigmore Land and Produce Co. Ltd. (91 ITR 476 Mad.), the court observed that the Tribunal had given a finding that the payment of gratuity was made in pursuance of the general practice adopted by the company and as a result there was an expectation by the employee of being paid gratuity. As the general practice of paying gratuity in respect of retired employees was established it was held to have sufficient nexus with future carrying on of the business as the expectation would act an inducement for the employees to hold on to the service till retirement and this will facilitate to carrying on by the employer of the business without any break or interruption.*

8) *In the case of Balarama Varma Textiles vs. CIT (92 ITR 485 Mad.), the court noted that adhoc gratuity paid to employees without such gratuity having any link with the length of service of such employees or salary drawn by them and without any uniform practice would not be an allowable business expenditure.*

9) *In the case of CIT vs. Laxmi Cement Distributors (P) Ltd. (104 ITR 711), the court found that voluntary gratuitous payment made to the daughter of an employee who died abroad while in service of the assessee company with a view to maintain good relations and to engender confidence of all the employees was held justified on ground of commercial expediency and allowable as business deduction.*

10) *In the case of CIT vs. Oxford University Press (108 ITR 166 Born.), the court noted that there was no scheme as such between the assessee-company and the covenant staff of the company. But a scheme of gratuity existed, as a result*

of settlement between the assessee company and non-covenant staff. As a result of such scheme gratuity paid to the covenant staff was held to be allowable as the covenanted staff could reasonably expect similar gratuity.

11) *In the case of CIT vs. Fairdeal Corporation Pvt. Ltd. (108 ITR 280 Born.), the court noted that there was no evidence on record to show that there was any established practice in the assessee's company to pay gratuity to its directors. However, gratuity paid to the widow on the death of the managing director was held to be allowable on grounds of commercial expediency as it was found that the managing director foregone his salary for earlier 2 years due to the loss incurred by the assessee company and as the payment was not made on any adhoc basis but on the basis of 15 days of sales for each completed year of service. The payment was held to be made not only in recognition of his past services but also on grounds of commercial expediency.*

12) *In the case of CIT vs. Patel Cotton Co. Pvt. Ltd. (108 ITR 846 Born.), the assessee company has taken over similar business of another company the employees of the other company were absorbed by the assessee. There was a system of payment of gratuity to the employee of the assessee company at the time of takeover. Payment of gratuity to the employees of the taken over company was held to be ensured to retain the staff working already and contentment among them and was held to be commercially expedient. The court opined that the tests laid down by the Supreme Court are satisfied and hence the payment was allowable as deduction.*

13) *In the case of CIT vs. Glaxo Laboratories (India) P. Ltd. (114 ITR 110), payment was found to have been made upon termination of selling agency with a view to maintain goodwill and for the smooth transition from agency distribution to direction distribution and to avoid the agent from creating nuisance and such payment was held to be deductible as it was found to have been made in the interest of business to avoid any hindrance from the selling agent.*

14) *In the case of CIT vs. Chloride & Exide Batteries (P) Ltd (114 ITR 0142) the assessee company paid gratuity to its manager on his retirement. The department disallowed the dam stating that there was no practice of payment of gratuity to the entire staff and that there was no contractual obligation to pay any gratuity to the manager and that it was not established that the payment was made exclusively out of business consideration. However, Tribunal had given, a finding that there was a practice in the company of payment of gratuity and during the currency of services the manger was informed that he will be paid gratuity and*

accordingly a resolution sanctioning payment of gratuity was passed by the Board and therefore the court found that the test of expectation has been directly satisfied and the test of commercial expediency was also indirectly satisfied. The court reviewed an the earlier decisions referred above and followed the view taken by the Andhra Pradesh High Court in the case of British India Tobacco Corpn. Ltd. vs. CIT (79 ITR 41) and the Bombay High Court decision in the case of CIT vs. Oxford University Press (108 ITR 166) holding that the tests laid down by the Supreme Court are disjunctive and alternative. The court also noted that even without any expectation that similar payments in certain cases have been held to be commercial expedient in the case of CIT vs. Laxmi Cement Distributors Pvt. Ltd.(1978FR Bombay 815) and CIT vs. Fairdeal Corporation Pvt. Ltd (108 ITR 280).

15) *In the case of Sasoon J. David & Co. P. Ltd. vs. CIT (118 ITR 261 SC), the expenses incurred by way of retrenchment compensation paid to the directors and employees as per the agreement of transfer of shares was found to the benefit of the company's business and hence allowable as a deduction. The court opined that the expression 'wholly and exclusively" used in s. 10(2)(xv) does not mean 'necessarily. Ordinarily it is for the assessee to decide whether any expenditure should be incurred in the course of his or its business. Such expenditure may be incurred voluntarily and without any necessity and it is incurred for promoting the business and to earn profits, the assessee can claim deduction even though there was no compelling necessity to incur such expenditure. The fact that somebody other than the assessee is also benefited by the expenditure should not come in the way of an expenditure being allowed by way of deduction under S. 10(2)(xv) if it satisfies otherwise the tests laid down by law. In the instant case, it was the case of We company that many of the employees were old and superfluous and the business could be carried on with a smaller number and the only way in which they could reduce the number was to terminate the se, vices of all the employees by paying them ompensation and thereafter reemploying some of them only. If the company felt that was a method which would enure to its benefit, it cannot be said that the payment of compensation was made with an oblique motive and without regard to commercial consideration or expediency. Hence, amount paid to directors and employees is allowable as a deduction.- Sasoon J. David & Co. (P) Ltd. vs. CIT (1972) 85 ITR 83 (Bom) : TC16R.331 and Sasoon J. David & Co. P. Ltd. vs. CIT (1975) 98 ITR 50 (Born) partly reversed; Gordon Woodroffe Leather Manufacturing Co. vs. CIT (1962) 44 ITR 551 (SC) : TC16R.1378 and CIT vs. Chandulal Keshavlal &*

Co. (1960) 38 ITR 601 (SC) : TC16P.507 applied; CIT vs. Laxmi Cement Distributors P. Ltd. 1976 CTR (Gui) 338 : (1976) 104 ITR 711 (Guj) : TC1 6R. 434, CIT vs. Fairdeal Corpn. P. Ltd. 1977 CTR (Born) 815: (1977) 108 ITR 280 (Born): TC16R.1457#1 and CIT vs. Patel Cotton Co. Pvt. Ltd. 1976 CTR (Born) 1 : (19 77) 108 ITR 846 (Born) : TC16R.1457 impliedly approved.

16) *In the case of CIT vs. Globe Theatres Pvt. Ltd. (122 ITR 240 Born.) the pension paid to the widow of the one of the directors was not allowable as deduction as it was not incurred wholly and exclusively for the purpose of business. The court noted that the widow rendered no service to the company, there was no basis of arriving the amount of monthly payment to them and such payment could not be equated with the gratuity or family pension paid to the widow of an ordinary employee without who had served the company for a long.*

17) *In the case of CIT vs. Herbert Sons P. Ltd. (124 ITR 613), pension was paid to a retired employee who has served the company for more than 30 years. There was no scheme for payment of pension but it was found that a gratuity scheme was introduced in the year 1957 during which the retired employee was serving in the company. Therefore he had a reasonable expectation that the company will give some kind of retirement benefit. Therefore a view was taken that the payment was made in lieu of benefit available under the gratuity scheme. Considering all these circumstances, the court held that the payment cannot be said to be purely voluntary payment. The employee was expecting some benefit for his long and faithful services to the company. Therefore the payment is allowable.*

18) *In the case of CIT vs. Srinivasa Perumal Bank Ltd. (131 ITR 692 Mad.), the court held that payment of gratuity to the employee on the resignation from services as part of an agreement of merger is deductible even though the payment was made after closure of business.*

19) *In the case of CIT vs. Commonwealth Trust Ltd. (166 ITR 732 Ker.), pension payment made to employees was held to be not deductible when there was no scheme of payment of pension at the time of retirement when the employee had no expectation of receiving pension while in service and the payment was not paid as a matter of fact effecting quantum of salary received while in service. The payment was also not found to be commercial expedient.*

20) *In the case of CIT vs. Indian Molasses Co. (P) Ltd. (166 ITR 740 Cal.), the court noted that where the employee at the inception of his service had given to understand that he would be entitled to pension when he retires; the provision for payment to widow was held to be expended wholly for*

the purpose of business.

21) *CIT vs. Hindustan Motors Ltd. (175 ITR 411), the court held that the existence of general pension scheme is not always conclusive; each case depends on its own facts. If the payment to the widow of a deceased employee or retired employee is found to be gratuitous and not on account of any practice or commercial expediency, the same will not be allowed.*

22) *In the case of Travancore Rubber & Tea Co. Ltd. vs. State of Kerala(239 ITR 351 Ker.), the court held that any expenditure incurred on employees to keep them in good stead is for commercial expediency.*

23) *In the case of CIT vs. Lucas Indian Services Ltd. (239 ITR 429), a resolution was passed by the assessee company granting benefit of pension to the widow of former director. The resolution was passed when the director was working for the purpose of company. The court found that there was all expectation in the mind of the employee the pension payment will be made to him and after his demise to his legal heirs The payment was made only to generate confidence in the mind of the employee that he would be taken care after his retirement and after his demise his legal heirs, would taken care of. This would promote good relationship between the employer and the employees. Therefore the' payment was held to be commercially expedient.*

14 The various judicial decisions discussed in the earlier paras lay down the following principles:

14.1 Expenditure incurred voluntarily without any legal obligation or compelling necessity would be allowable deduction if they are incurred out of business considerations and commercial expediency. The expenditure should not have been incurred for any improper, oblique purpose. The payment should have clear nexus to commercial expediency. There should be direct and intimate connection between expenditure and business. The expenditure incurred even if indirectly facilitates the business would be an allowable deduction. It is not necessary that the payment should result in direct benefit or earning of immediate profit. The element of commercial expediency has to be determined in regard to facts and circumstances in each case, and it is the businessman, who is the best judge to determine what are the expenses to be incurred for his business.

14.2 In regard to payment of 'gratuity' or 'pension' to ex-employees, the Hon'ble Supreme Court has laid down the following test:

Was the payment made as a matter of practice with effected the quantum of salary or was there an expectation by the employees of getting 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.

14.3 The Andhra Pradesh High Court in the case of British India Tobacco Corporation Ltd. vs. CIT he'd that the tests laid down by the Supreme Court in Gordon Woodroff are disjunctive and alternative. Similar view was expressed by the Gujarat High Court in the case of CIT vs. Chloride and Exide Batteries P Ltd. (114 ITR 142). Thus, if any one of the tests, laid down by the Supreme Court in Gordon Woodroffe are satisfied, the deduction towards gratuity would be allowable. If none of the conditions are satisfied then the claim of deduction has to be disallowed. Wherever there is a scheme for payment of gratuity or where there was an expectation of the employee to get such gratuitous benefit, the payments were held to be allowable. In the case of CIT vs. Laxmi Cement Distributors (1978 CTR Bonn. 815), and CIT vs. Fair Deal Corporation Pvt. Ltd. (108 ITR. 280), the court have allowed deduction even when there Was no such expectation on grounds of business expediency. The decisions in the case of CIT vs. Fair Deal Corporation (108 TR 280) and CIT vs. Laxmi Cement Distributors Pvt. Ltd. (104 UR 711) were impliedly approved by the Hon'bleSupreme Court in Sasoon 3 David & Co. P. L. vs. CIT (117 ITR 261 SC). Payments made to avoid industrial unrest to promote good relationship between employer and employee were held to be commercially expedient.

14.4 In the light of the various guidelines and criteria laid down in the above judicial decisions it has to be seen whether the impugned payments are allowable u/s37(1) of the I.T. Act.

14.5 As per the Board resolution the impugned ex-gratia lump sum payments have been made in pursuance of the commitment made by the chairman of the company to its ex-workers and staff to provide some financial support as gratitude towards their continuous services rendered and extended during the critical situations of the company. It was also submitted that the payments have been made proportionate to the services rendered by them with the assessee and subsequently with the lessees. The said resolution was preceded by request letters from the employees and communication from the Lessee advising to settle so as to avoid any likely industrial unrest. The AO has doubted the veracity of these letters as only ten letters were sent which were in same hand writing and they were not sent through the Union. In this context it

is relevant to note that the Plant Manager and the Lessee have also sent communication about impending demands and expectations of the labourers, which were not questioned. Therefore, I am of the view that there is no material basis to doubt the veracity of these communications.

14.6 With the Leasing of the units, the assessee cease to be an employer in relation to these workmen. From the perusal of the Common Award passed by the Labour Court Cum Industrial Tribunal in ID No.243/98 & ID No.181/1999 it is seen that there were two employees union and that the employees affiliated to the Vasavi Jute Twine Workers Union did not raise any dispute against the management This shows that a section of the employee /workmen have stood by the management during the period of unrest, and therefore it is possible to infer that the chairman had made certain commitments to the employees who would continue to work in the assessee's jute mills. Though there is no direct evidence as to commitment made by the chairman, the facts on record indicating that some section of employees supported the management and many of the employees continued to work with the different Lesseeses of the assessee company would be a fair indication to infer of such commitment. The expectations of the employees are evident from the communications of the employees, the Plant Manager and the Lessees."

24. The ld. CIT(A) further considered that there is a business expediency in making the impugned lump sum payments that the cooperation of employees are crucial for smooth function of the mills and the assessee cannot remain oblivious to the employees expectations even though the factories have been leased out. It is also evident that some section of the employees have extended their support during the critical times, and the management reciprocating such cooperation through *exgratia* payment for their past and continuous service would go to improve the good relationship between the employer and employees, and resulting

cordial working environment would prove advantageous to the assessee's business. Thus, it can be said that the payment of the impugned amounts have direct bearing and sufficient nexus to the assessee's business. He relied on the decision of the Hon'ble Kerala High Court in the case of *Travancore Rubber & Tea Co. Ltd. vs. State of Kerala* and also the decision of the Hon'ble Supreme Court in the case of *Delhi Safe Deposit Co. Ltd.,* (133 756). The ld. CIT(A) has considered that the assessee has paid *exgratia* lump sum payment to 333 employees and staff of Rs. 97,47,042/- during the year. Out of these, 83 employees have not continued their employment with the lessee of assessee's company and they have left assessee's employment as on 16/02/1998, the payment made to these 83 employees amounted to Rs.12,29,167/-. As per Board Resolution, the lump sum exgratia are paid to those who have rendered services with the assessee and subsequently with the lessee. Thus, these payments are not in accordance with the resolution passed by the Board. It is submitted before the ld.CIT(A) that the above payments are made as per the commitment made by the management as these employees did not participate in the litigation with Labour court. The assessee has not filed any evidence in support of such commitment and

therefore the ld.CIT(A) has disallowed to the tune of Rs.12,29,167/- and to that extent, order passed by the Assessing Officer is upheld. On similar footing is the payment to the employees in S.No. 284 of Rs. 28,333/- and S.No.299 of Rs.38,333/- also disallowed. On similar lines, payments made to S.No. 306 of Rs. 20,000/- is also disallowed. The ld. CIT(A) further observed as under:-

> *"14.11 It is also relevant to note that the AO in the impugned order referred to some of the employees whose services are less than 10 to 11 years and would not fall under the scheme of payment. It is seen that most of such employees are covered in the disallowance made above of Rs. 12,29,167/-. However, it is seen that employees referred in the assessment order with reference to Sl.No. 146, 65, 314, 199,149,267, 259 & 330 are found to have joined employment from 1998 onwards and as a result the period of service is less in these cases.*
>
> *14.12 It may be noted that in the proposal for lumpsum exgratia payment, "INTUC Vasavi Workers working outside" were also covered and considered as eligible. The authorized representative was asked to clarify what does 'working outside' mean. It was stated that these workmen are not regularly employed by the assessee and are kept on temporary basis. Thus admittedly these category of workers are also not employed with the lessee company and have not continued their services with the assessee company and therefore such payments would not fall within the purview of the conditions stated in the Board resolution. The element of continuity of service is lacking and as such no business expediency has been made out. Therefore, the AO may disallow the payments made to these category of employees after due verification. Necessary care may be taken to avoid double disallowance. The payments other than those referred in para 14.10 & 14.12 above included in the impugned amount of Rs.97,47,082/- may be allowed."*

25. Before us, ld. Departmental Representative has submitted that lump sum *exgratia* payments made by the assessee are not

arising out of the contractual liability hence, the same cannot be allowed and strongly supported the order passed by the Assessing Officer.

26. On the other hand, ld. Authorized Representative for the assessee has submitted that the management committed to pay these payments keeping in view of the long service of the employees and also continuing their services with the different lessees and extending their support during the critical days. Keeping in view of the difficulty in getting skilled workers in jute industry, it is submitted alternatively that it is the commercial expediency of the assessee to pay these amounts to safeguard the business needs of the assessee company.

27. We have heard both the sides, perused the material available on record and orders of the authorities below.

28. We find that the assessee has paid lump sum *exgratia* payments to the employees of Rs. 97,47,042/-. The case of the Assessing Officer is that there is no contractual liability on the part of the assessee to pay these payments to the ex-employees of the assessee-company. It is also not a statutory obligation on the part of the assessee to make these payments, therefore, he disallowed the same. On appeal, ld. CIT(A) has considered

various documents and minutes of the Board meetings, representations made by the workers and letters from the employees for request to financial help and also by considering the various case laws. It is also submitted that the above payments are made as per the Board resolution in pursuance to the Chairman of the company to its ex-workers and staff to provide some financial support as gratitude towards their continuous service rendered and extended support in critical situation of the company. The ld. CIT(A) has considered the above submissions and gave a categorical finding that though there is no direct evidence for commitment made by the Chairman, the facts on record indicating that some section of the employees supported the management and many of the employees continued to work with the different lessees of the assessee company, would be a fair indication to infer of such commitment. The expectations of the employees are evident from the communications of the employees, the Plant Manager and the lessees. The ld. CIT(A) by considering various judgments of the Hon'ble Supreme Court and different High Courts, came to a conclusion that these payments are made by the assessee are allowable under section 37(1) of the Act.

29. The ld. CIT(A) has also considered the decision of the Hon'ble Supreme Court in the case of *Delhi Safe Deposit Co. Ltd.* (supra) and also the decision of the Hon'ble High Court of Kerala in the case of *Travancore Rubber & Tea Co. Ltd.* (supra) and observed that these lump sum payments are made by the assessee for the business expediency of the assessee and therefore, it is allowable under section 37 of the Act. The very same issue of business expediency has been considered by us in this order in page Nos.36 & 37 at para Nos. 16 & 17. The findings given in the above paragraphs are even applicable for lumpsum *exgratia* payments also.

30. We have considered the detailed order passed by the ld.CIT(A). He brought all the material on record and also considered the various judicial pronouncements and came to a conclusion that the lumpsum exgratia payments are made by the assessee are allowable under section 37 of the Act. We find that ld. Departmental Representative has not brought anything on record to show that the findings given by the ld. CIT(A) are not correct and the also case laws relied on by the ld. CIT(A) are not relevant. By considering the facts and circumstances of the case, we are of the opinion that the ld. CIT(A) has discussed the issue

elaborately and decided by following various judicial pronouncements of the Hon'ble Supreme Court and also different High Courts, the claim to the extent of Rs.84,31,249/- is allowed and Rs.13,15,838/- is confirmed. We find no reason to interfere with the order passed by the ld. CIT(A). Thus, this appeal filed by the Revenue is dismissed.

ITA No. 349/VIZ/2016

31. So far as assessee's appeal is concerned, the total disallowance made by the Assessing Officer is of Rs. 17,74,205/-. So far as *exgratia* payment of Rs. 13,15,833/-, the ld. CIT(A) gave a categorical finding that the employees are already left the employer of the lessee company and there is no business expediency to make these payments. The assessee also failed to adduce any evident in support of commitment made to the employees, therefore, ld. CIT(A) has disallowed the above amounts. We find no infirmity in the order passed by the ld.CIT(A) on this count.

32. So far as Children Education Allowance of Rs. 1,22,940/- is concerned, the assessee is not proved the business expediency to make these payments and therefore ld. CIT(A) directed to disallow the above amount of Rs. 1,22,940/-. Before us except stating

that the above payments are made for business expediency, but no proof of business expediency is filed. Therefore, we find no infirmity in the order passed by the ld. CIT(A) on this count.

33. So far as festival bonus of Rs. 4,500/- and other staff welfare expenses of Rs. 3,30,932/- are concerned, the ld. CIT(A) is of the opinion that there is no basis for the above amounts paid and also there is no business expediency, therefore the same is disallowed. The assessee has also not produced any evidence to substantiate the above amounts paid by the assessee to the ex-employees for the business expediency. Therefore, we find no infirmity in the order of the ld. CIT(A).

ITA No. 458/VIZ/2017

34. The issues involved in this appeal are similar to the issues of Assessment Year 2012-13. The ld. CIT(A) at page No. 29 of his order, gave a categorical finding that the facts and issues involved in the allowability of these expenditure was identical to those in the assessee's case for the Assessment Year 2012-13. We also find that the facts and issues are similar. The Departmental Representative as well as ld. Authorised Representative for the assessee has submitted that in the light of the Assessment Year 2012-13, this appeal may be disposed of.

35. The assessment year under consideration, the assessee has claimed Rs. 35,96,735/- towards children education allowance. On verification of the details filed by the assessee, the ld. CIT(A) has disallowed Rs. 1,62,310/- on the ground that the assessee has not proved the business expediency in making these payments.

36. So far as payment of Rs. 23,21,472/- towards exgratia/ festival bonus, the assessee is failed to prove the business expediency of Rs. 28,383/-, hence, ld. CIT(A) allowed only Rs.22,93,086/-. The Assessing Officer has disallowed Rs.6,90,933/- on the ground that these payments are not in pursuance to the scheme and also no business expediency. The assessee only filed payment particulars before the ld. CIT(A) without filing any supportive evidence to show that these expenditure were incurred for the purpose stated in accordance with the scheme. Therefore, ld. CIT(A) has disallowed the same.

37. So far as lumpsum *exgratia* payment of Rs. 97,17,082/- is concerned, the ld. CIT(A) by following his own order in Assessment Year 2012-13 in ITA No. 109/2015-16/CIT(A)-2/VSP/ ITO/W-3/SKL/2016-17, dated 28/04/2016 disallowed Rs.12,47,083/- on the ground that the payments made to 80

employees, amounting to Rs. 11,85,000/-, discontinued their employment with the assessee company on 16/02/1998 i.e. after the strike of the mill and leasing of the unit. The ld. CIT(A) has observed that there is no element of business expediency or any justification for the above payment to that extent, the ld. CIT(A) directed the Assessing Officer to disallow these payments. With regard to payments of Rs. 38,333/-, Rs. 20,000/- & Rs. 38,333/-, ld.CIT(A) gave a categorical finding that the above payments made are not in accordance with the resolution of the Board and there is no business expediency because some of the employees discontinued their employment soon after the leasing out the unit. We find that there is no infirmity in the order passed by the ld.CIT(A). Therefore, keeping in view of the facts and circumstances of the case and also the order passed by the ld.CIT(A) in Assessment Year 2012-13 is upheld by the tribunal, we find no reason to interfere with the order passed by the ld.CIT(A) for Assessment Year 2013-14. Thus, this appeal filed by the revenue is dismissed.

ITA No. 404/VIZ/2017

38. So far as assessee's appeal is concerned, facts and circumstances are similar to that of Assessment Year 2012-13.

We also find that ld. CIT(A) has given a specific reason for disallowance of Rs. 12,47,083/- in respect of exgratia payment; Rs. 1,62,310/- in respect of Children Education Allowance; Rs.28,386/- in respect of festival bonus and Rs. 6,90,933/- in respect of other staff welfare expenses that these amounts paid are not in accordance with the scheme and also payments are made to the employees who are left the assessee company. The ld. CIT(A) has considered the Board Resolution as well as business expediency and came to a conclusion that there is no Board Resolution and also no business expediency. Accordingly, he disallowed the same. We find no reason to interfere with the order passed by the ld. CIT(A). Thus, this appeal filed by the assessee is dismissed.

39. In the result, appeals filed by the Revenue in ITA Nos.340/VIZ/2016 & 458/VIZ/2017 as well as appeals filed by the assessee in ITA Nos.349/VIZ/2016 & 404/VIZ/2017 are **dismissed**.

Order Pronounced in open Court on this 09th day of Feb., 2018.

Sd/-	sd/-
(D.S. SUNDER SINGH)	**(V. DURGA RAO)**
Accountant Member	**Judicial Member**

Dated : 09th February, 2018.

vr/-

Copy to:

1. *The Assessee* – M/s. Sri Varalakshmi Jute Twine Mills Pvt. Ltd., Bobbili Road, Rajam (PO), Srikakulam District.
2. *The Revenue*
   a. *ITO, Ward-3, Srikakulam.*
   b. *ACIT, Circle-4(1), Visakhapatnam.*
   c. *DCIT, Circle-4(1), Visakhapatnam*.
3. *The CIT-2, Visakhapatnam.*
4. *The CIT(A)-2, Visakhapatnam.*
5. *The D.R., Visakhapatnam.*
6. *Guard file.*

By order

(VUKKEM RAMBABU)
Sr. Private Secretary,
ITAT, Visakhapatnam.