C.W.S. (INDIA) LIMITED

v.

THE COMMISSIONER OF INCOME TAX

MARCH 1,1994

[B.P. JEEVAN REDDY AND B.L. HANSARIA, JJ.]

Income tax Act, 1961: Sections 40(c)(iii), 40(a)(v) & 40A(5)—Section 40(a)(v) in force upto 31-3-1972—Section 40A(5) substituted with effect from 1.4.1972—Interpretation of the provision—Amenities or perquisites to employees beyond a particular limit—Disallowance of—Whether valid.

Interpretation of Statutes: Objects of all the rules of interpretation is to give effect to the object of the enactment having regard to the language used—Interpretation not a mechanical exercise.

Section 40(a)(v) of the Income tax Act, 1961 was in force till 31.3.1972. It was substituted by Section 40A(5) with effect from 1.4.1972. Both provisions were substantially similar. The two provisions were in force successively form April 1,1963 to March 31,1989. These provisions were enacted with a view to discourage the assessees from incurring expenditure which resulted directly or imdirectly in the provision of any benefit, amenity or perquisite to their employees beyond a particular limit. Any expenditure beyond the prescribed limite was disallowed.

In the present appeals, such disallow were challenged, raising questions relating to the interpretation of Section 40(a)(v)

Dismissing the appeals, this Court

HELD: 1.1. While literary construction may be the general rule in construing taxing enactments, it does not mean that it should be adopted even if it leads to a discriminatory or incongrous result. Interpretation of statutes cannot be a mechanical exercise. Object of all the rules of interpretation is to give effect to the object of the enactment having regard to the language used. [254-E]

1.2. Section 40(a)(v) of the Income tax Act, 1961 is only and expanded version of Section 40(c)(iii). The idea was to bring the allowances in respect of the assets owned by the assessee, which assets are used by its

A employee for his own purposes or benefit, within the net of ceiling. Section 40(c)(iii) did not cover such allowances and this was sought to be remedied. The idea was certainly not to bring about a different treatment of two situations in Section 40(a)(v). The consequence of accepting the assessee's interpretation would be that while the ceiling on expenditure would apply to a certain case, no such ceiling would apply to certain other B cases. The consequence would not only be discriminatory but also very incongruous, almost absurd. In principle, there is no distinction between the two cases or the two situations, as they may be called. Mere use of the word "such" should not have the effect of driving the court to place an interpretation upon the said clause which is not only discriminatory but C is highly incongrous. [254-A-D]

Commissioner of Income-tax, Kerala-I v. *Travancore Tea Estates Co. Ltd.*, 122 I.T.R. 557, approved.

Commissioner of Income-Tax v. *Forbes, Ewart and Figgies(P) Ltd.*, 138 D I.T.R.1, disapproved.

Maxwell's *'Interpretation of Statutes'* (12th Edn.), referred to.

2. So far as Section 40A(5) is concerned, controversy does not and E cannot arise for the reason that the second part of clause (ii) in sub-section (5) does not use the words "such employee" but uses the words "an employee". It is not without signigificance that while substantially repeating the provision in Section 40(a)(v) in Section 40A(5)(a)(ii), the Parliament has taken care to substitute the word "such" with the word "an". [255-F]

F 3. Both Sections 40(a)(v) and 40(5)(a)(ii) speak of "any allowance in respect of any assets of the assessee used by an employee". The asset may be a building, a car, a refrigerator or an air-conditioner or any other asset. The allowance in respect of such assets certainly means and includes depreciation allowance on such assets. [255-H; 256-A]

G 4. In respect of the other question urged *viz.* that amount expended on repairs is not includible in the expenditure referred to in Sections 40(a)(v) and 40A(5)(a)(ii), it does not appear from the order of the High Court that the said question was either referred to it or was answered by it. Therefore, this Court declines to go into the said question. However, in H respect of this question the relevant appeals shall subsist and shall be

heard along with pending Civil Appeal No. 8168 of 1988 (Industrial Chemicals v. Commissioner of Income tax). [256-A-B] A

CIVIL APPELLATE JURISDICTION: Civil Appeal Nos. 677-82 of 1987.

From the Judgment and Order dated 13.9.85 of the Kerala High Court in I.T.R. Nos. 55-60 of 1982. B

WITH

C.A. Nos. 493-98/84, 487-92/84, 50180-21/91 and 4614-16/93.

C

From the Judgment and Order dated 2.6.81, 11.9.91, 7.12.89 and 27.1.89 of the Kerala High Court in I.T.R. Nos. 76, 79 to 82/78, 44/79, O.P. Nos. 9261-62, 9329-34/89, and I.T.R. Nos. 376-77/85 and O.P. No. 3373 of 1988-S.

G.B. Pai, R.F. Nariman, Mrs. A.K. Verma, D.N. Mishra, (for M/s J.B.D. & Co.), S. Balakrishnan, M.K.D. Namboodry, K.J. John and Joseph Joy for the Appellants D

K.N. Shukla, Dr. K.P. Bhatnagar, T.V. Ratnam for B. Krishna Prasad for the Respondent.

E

The Judgment of the Court was delivered by

B.P. JEEVAN REDDY, J. *CIVIL APPEAL NOS. 493-98 OF 1984.*

A common question arises in this batch of appeals. It pertains to the interpretation of Section 40(a)(v) as well as Section 40A(5) of the Income Tax Act. Upto March 31, 1972, Section 40A(5) came into force and from April 1, 1972, Section 40A(5) came into force in its place. Both the provision were substantially similar. Indeed, Section 40(a)(v) was preceded by Section 40(c)(iii) which was, of course, applicable only to companies and not to other assessees. F G

Section 40 (c)(iii) introduced by Finance Act, 1973 with effect from April 1, 1963, as substituted by Finance Act, 1964, read as follows:

> "*40. Amounts not deductible:* Notwithstanding anything to the contrary in Sections 30 to 38, the following amounts shall not be H

A deducted in computing the income chargeable under the head "profits and gains of business of profession"--

(c) in the case of any company--

"(iii) any expenditure incurred after the 29th day of February, 1964 B which results directly or indirectly in the provision of any benefit or amenity or perquisite, whether convertiable into money or not, to an employee (including any sum paid by the company in respect of an obligation which but for such payment would bave been payable by such employee), to the extent such expenditure exceeds C one-fifth of the amount of salary payble to the employee for any period of his employment after the aforesaid date:

Provided that in computing the aforesaid expenditure any payment by way of gratuity or the value of any travel concession or assistance referred to in clause (5) of section 10 or passage moneys D or the value of any free or concessional passage referred to in sub-clause(i) of clause (6) of that section or any sum referred to in clause (viii) of sub- section (i) of section 17 or in clause (v) of sub-section (2) of that section or the amount of any compensation referred to in clause (i) or any payment referred to in clause (ii) of sub- section (3) of that section or any payment referred to in E clause (iv) or clause (v) of sub section 1 of section 36 shall not be taken into account."

By Finance Act, 1968, sub-clause (iii) in clause (c) of Section 40 was deleted and in its place sub-clause (v) was introduced in clause (a) of F Section 40. As introduced by the said Finance Act, the sub-clause read as follows:

"40. Amounts not deductible: Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall be deducted in computing the income chargeable under the head G "profits and gains of business of profession"–

(a) in the case of any assessee–

(v) any expenditure which results directly or inderectly in the provision of any benifit or amenity or perquisite, whether convert- H ible into money or not, to an employee (including any sum paid

by the assessee in respect of any obligation which but for such payment would have been payable by such employee) or any expenditure or allowance in respect of any assets of the assessee used by *such employee* either wholly or partly for his own purposes or benefit, to the extent such expenditure or allowance exceeds one-fifth of the amount or salary payable to the employee, or an amount calculated at the rate of one thousand rupees for each month or part thereof comprised in the period of his employment during the previous year, whichever is less,"

(Emphasis supplied)

(Provisos (1) & (2) and Explanations (1) and (2) - omitted as unnecessary).

This sub-clause is applicable to all assessees including companies. By virtue of the first proviso, this clause does not apply where the income chargeable under the head "salaries" of the employee concerned is Rs.7,500 or less. Explanation (II) says that the word "salary" in this clause shall have the meaning assigned to it in Rule 2(h) of Part-A of the Fourth Schedule to the Act.

With effect from April 1, 1972, Section 40A(5) was introduced in substitution of Section 40(a)(v). As introduced by Finance Act, 1971, it read as follows:

"40A. Expenses or payments not deductible in certain circumstances:-

(5)(a) Where the assessee–

(i) incurs any expenditure which results directly or indirectly in the payment of any salary to an employee or a former employee, or

(ii) incurs any expenditure which results directly or inderectly in the provision of any perquisite (whether convertible into money or not) to an employee or incurs directly or indirectly any expenditure or is entitled to any allowance in respect of any assets of the assessee used by an employee either wholly or partly for his own purposes or benefit, then subject to the provisions of clause (b), so much or such expenditure or allowance as is in excess or the limit specified in respect thereof in clause (c) shall not be allowed

A as a deduction:

Provisos (1) and (2) - (omitted as unnecessary).

Clauses (b) and (c) - (omitted as unnecessary).

B Explanations (1) and (2) - (omitted as unnecessary)."

The sub-section has been amended later in certain respects, but it is not necessary to notice them for the purpose of these cases. The sub-section has been omitted altogether by Direct Tax Law (Amendment) Act, 1987 with effect from April 1.1989.

C

The provision aforesaid, which were in force successively from April 1, 1963 to March 31, 1989, were enacted with a view to discourage the assessees from incurring expenditure which resulted directly or indirectly in the provision of any benefit, amenity or perquisite to their employees beyond a particular limit. Any expenditure incurred beyond the prescribed D limit was disallowed. The first and the main controversy in these appeals pertains to the interpretation of Section 40(a)(v), to which we may now turn.

The main limb of clause (v) spoke of two situations, *viz.*, (i)where an assessee incurred any expenditure which resulted directly or indirectly E in the porvision of any benefit or amenity or perquisite whether convertible into money or not, to an employee (including any sum paid by the assessee in respect or any obligation which but for such payment would have been payable by such employee); and (ii) any expenditure incurred by an assessee in respect of any assets belonging to it and any allowance in respect of such assets, which were used by "such employee" either wholly F or partly for his own purposes or benefit. We shall refer to them hereafter as clauses (i) and (ii) for the sake of convenient reference. To both the above situations, the ceiling prescribed in the clause applied, the ceiling being 1/5th of the amount of the salary payable to the employee or an amount calculated @ one thousand rupees for each month, whichever was G less. (The first proviso stated that certain items shall not be taken into account in camputing the expenditure and allowance referred to in the main limb of the clause). It may be noticed that the two situations, which we have set out in the preceding paragraph as (i) and (ii), are linked by the word "or".

H The contention of the assessees, which was accepted by the Division

Bench of the Kerala High Court in *Commissioner of Income-Tax, Kerala-I* v. *Travancore Tea Estates Co. Ltd.,* 122 I.T.R. 557 but rejected by the Full Bench in *Commissioner of Income-Tax* v. *Forbes, Ewart and Figgies (P) Ltd.,* 138 I.T.R.1 is this: an employee using the assets of the assessee-employer for his own purposes and benfit falls within clause (ii); to such employee, the ceiling prescribed in clause (v) does not apply unless he is also in receipt of any benefit, amenity or perquisite mentioned in clause (i); this is for the reason that clause (ii) uses the expression "such employee" which can only mean an employee referred to in clause (i). Therefore, unless an employee is in receipt of any benefit, amenity or perquisite resulting from any expenditure incurred by the assessee within the meaning of clause (i), the ceiling prescribed in clause (v) will not apply to the expenditure incurred by the assessee over an asset - or to an allowance claimed by the assessee in respect of an asset - used by the employee for his own benefit within the meaning or clause (ii). The argument is built exclusively upon the words "such employee" in clause (ii).

We find it difficult to agree with the learned counsel for the assessees. The first thing to be noticed is that or the two clauses in sub-clause (v), clause (i) was already there in Section 40(c)(iii). If an asset belonging to the assessee - say, for example, a furnished house - was placed in possession and enjoyment of its employee and it was being maintained by the assessee, there could be little doubt that any expenditure incurred on such asset/house was subject to the ceiling prescribed therein. Similarly, if a house taken on rent by the assessee was furnished by the assessee and put in possession and enjoyment of its employee, the expenditure incurred in that behalf would equally have been subject to the ceiling in Section 40(c)(iii). Suppose, in another case, a house owned by the assessee (furnished and maintained by the assessee) is similarly placed in possession and enjoyment of the employee and the assessee took on rent an air-conditioner and installed in the said house, the whole expenditure would have been subject to the ceiling in Section 40(c)(iii). Now, the question is whether the Parliament intended differently when it put in Section 40(a)(v) in the place of Section 40 (c)(iii). In this connection , it may be noted that Section 40(a)(v) was in force from April 1, 1969 to March 31, 1972 only and that Section 40A(5) which came into force with effect from April 1, 1972 [in place of Section 40(a)(v)] does not admit of any such controversy in view of the fact that it uses the words "an employee" in the corresponding clause. Controversy is limited only to Section 40(a)(v) and only because of the use of the words "such employee".

A Now, it may be noticed that Section 40(a) (v) is only an expanded version of Section 40(c)(iii). The idea was to bring the allowances in respect of the assets owned by the assessee, which assets are used by its employee for his own purposes or benefit, within the net of ceiling. Section 40(c)(iii) did not cover such allowances and this was sought to be remedied. The idea was certainly not to bring about a different treatment B of two situations in Section 40(a)(v) referred to as clauses (i) and (ii) in this judgment. The consequence of accepting the assessee's interpretation would be that while the ceiling on expenditure would apply to a case falling under clause (i), no such ceiling would apply to a case falling under clause (ii) unless the employee governed by clause (ii) is also provided a benefit, C amenity or perquisite falling under clause (i). The consequence would not only be discriminatory but also very incongruous, almost absurd. In principle, there is no distinction between the two cases or two situations, as they may be called. We are satified that the mere use of the word "such" in clause (ii) should not have the effect of driving the court to place an D interpretation upon the said clause which is not only discriminatory but is highly incongruous. Sri G.B. Pai, learned counsel for the respondent-assessee, submitted that in case of taxing enactments, literary construction should be adopted and that the courts should not try to mould or twist the language of the enactment for achieving the supposed intention of the Parliament. While we agree that literary construction may be the gereral E rule in construing taxing enactments, it does not mean that it should be adopted even if it leads to a discriminatory or incongruous result. Interpretation of statutes cannot be a mechanical exercise. Object of all the rules of interpretation is to give effect to the object of the enactment having regard to the language used. The intention of the Parliament in enacting F Section 40(a)(v) can be gleaned from the memorandum explaining the provisions of the Finance Bill, 1968, which sets out the object behind this clause. The Full Bench of the Kerala High Court has set out the memorandum in the judgment under appeal. In this connection, we may refer to the well-recognised rule of interpretation of statutes that where a literal interpretation leads to absurd or unintended result, the language of the statute G can be modified to accord with the intention of Parliament and to avoid absurdity. The following passage from Maxwell's *'Interpretation of Statutes'* (12th Edn.) may usefully be quoted:

"1. MODIFICATION OF THE LANGUAGE TO MEET THE H INTENTION.

> Where the language of the statute, in its ordinary meaning and grammatical construction, leads to a manifest contradiction of the apparent purpose of the enactment, or to some inconvenience or absurdity which can hardly have been intended, a construction may be put upon it which modifies the meaning of the words and even the structure of the sentence. This may be done by departing from the rules of grammar, by giving an unusual meaning to particular words, or by rejecting them altogether, on the ground that the legislature could not possibly have intended what its words signify, and that the modifications made are mere corrections of careless language and really give the true meaning. Where the main object and intention of a statute are clear, it must not be reduced to a nullity by the draftsman's unskilfulness or ignorance of the law, except in a case of necessity, or the absolute intractability of the language used. Lord Reid has said that he prefers to see a mistake on the part of the draftsman in doing his revision rather than a deliberate attempt to introduce an irrational rule: "canons of construction are not so rigid as to prevent a realistic solution."

We are, therefore, of the opinon that the Full Bench of the Kerala High Court was right in taking the view it did on this aspect and we agree with it

So far as Section 40A(5) is concerned, the aforesaid controversy does not and cannot arise for the reason that the second part of clause (ii) in sub-section (5) does not use the words "such employee" but uses the words "an employee". It is not withourt significance that while substantially repeating the provision in Section40(a)(v) in Section 40A(5)(a)(ii), the Parliament has taken care to substitute the word "such" with the word "an".

Sri R.F. Nariman, learned counsel appearing for the assessee in Civil Appeal No. 4614-5 of 1993 raised two other contentions *viz*,. (i) the expression "allowance" in Section 40(a)(v) and Section 40A(5)(a)(ii) does not take in depreciation allowance; and (ii) that the amount expended on repairs is not includible in the expenditure referred to in the said provisions. So far as the first contention is concerned, it appears to be in the teeth of the language employed. Both Section 40(a)(v) and Section 40A(5)(a)(ii) speak of "any allowance in respect of any assets of the assessee used by an employee". The asset may be a building, a car, a

A refrigerator or an air-conditioner or any other asset. The allowance in respect of such assets certainly means and includes depreciation allowance on such assets. So far as second question urged by the learned counsel is concerned, it does not appear from the order of the High Court that the said question was either referred to it or was answered by it. We, therefore, B decline to go into the said question.

Civil Appeal Nos. 5018-21 of 1991:

Sri Balakrishnan, learned counsel for the assessee in these appeals, stated that of the two questions referred in these matters, the first question C was answered by the High Court against the assessee following the Full Bench decision in *Commissioner of Income Tax* v. *Forbes Ewart and Figgies Pvt. Ltd.* He says that the decision of this court on the said question in the connected appeals would govern the first question. But so far as the second question is concerned, he submitted that similar question arising in other cases have already been referred to a three-Judge Bench. Counsel, says D that those matters are still pending before this court. In view of the opinion expressed by us on the interpretation of Section 40(a)(v) and in view of the further circumstance that there is no room for such controversy in the light of the language used in Section 40A(5) ,the appeals are dismissed to the extent of first question. So far as the second question is concerned, the E appeals shall subsist and shall be heard alongwith Civil Appeal No.8168 of 1988 (*Industrial Chemicals* v. *Commissioner of Income Tax*), which appeal we are told involves a question identical to the second question arising in these appeals.

For the above reasons, all the appeals except Civil Appeal Nos.5018- F 21 of 1991 are dismissed. No costs.

Civil Appeal Nos. 5018-21 of 1991 are dismissed to the extent of first question [relating to Section 40A(5)] but shall subsist with respect to the second question and shall be heard along with Civil Appeal No.8168 of G 1988 (*Industrial Chemicals* v. *Commissioner of Income Tax*).

G.N. Appeal dismissed.