

A THE C.I.T., GUJARAT-I, AHMEDABAD  
v.  
THE AHMEDABAD COTTON MFG. CO. LTD. & ORS.

OCTOBER 15, 1993

B [B.P. JEEVAN REDDY AND N. VENKATACHALA, JJ.]

*Income Tax Act, 1961 : Section 37.*

C *Business expenditure—Company—Payment made to Textile Commissioner, in exercise of option under Clause 21-c(1)(b) of Textile Control Order, 1948, instead of producing and packing minimum quantity of specified cloth—Nature of—Payment made to Textile Commissioner, in terms of option under the terms of the bond, for not fulfilment of export obligation—Nature of—Held business expenditure—And not penalty.*

D A Textile Mill was being run by the assessee-Company, (In C.A. No. 2149 of 1977), during the accounting year 1971-72 previous to the Assessment Year 1972-73. The assessee, being a manufacturer of cotton textiles, had to comply with the directions issued from time to time by the Textile Commissioner under the provisions of the Cotton Textiles (Control)  
E Order, 1948, in the matter of producing and packing minimum quantity of specified type of cloth by it during the accounting year. However, the assessee instead of producing and packing the minimum quantity of specified type of cloth as required by the directions of the Textile Commissioner, paid to the Textile Commissioner Rs. 1,70,766 in exercise of the  
F option available to it under Clause 21-C(1)(b) of the Control Order. So also, the assessee, which had not fulfilled its export obligation under a bond entered into as regards exporting certain quantity of sanforized cloth paid to the Textile Commissioner Rs. 5,17,781 for non-fulfilment of that obligation, in exercise of its option available under the terms of the bond.  
G Thereafter, when the assessee filed its income-tax return relating to the accounting year 1971-72 with the jurisdictional Income Tax Officer, if claimed deduction of both the said amounts out of its profits, as business expenditure. The Income Tax Officer refused to allow the claimed deductions, taking the view that the said amounts paid by the assessee were not deduction which could be allowed as items of its business expenditure. On  
H appeal the Appellate Assistant Commissioner, allowed the amounts

claimed by the Assessee as items of its business expenditure in respect of its accounting year 1971-72. Revenue's appeal filed against that appellate order before the Tribunal did not meet with success. However, at the instance of the Revenue the Tribunal made a reference to the High Court under Section 256(1) of the Income Tax Act. The High Court upheld the claims of the assessee-Company. Similar orders were passed by the High Court in the connected appeals also. Against the decision of the High Court Revenue preferred appeals in this Court.

Dismissing the appeals, this Court

**HELD : 1.** It is ture, that a payment made by an assessee doing business in the accounting year is not entitled to claim deduction under Section 37 of the Income Tax Act, 1961 of an amount paid by such assessee during the year as an amount of penalty or an amount akin to penalty for any breach or infraction of law or any public policy which is sought to be achieved by such law. But if such payment is made by the assessee during the relevant accounting year without any breach of infraction of any law or any public policy sought to be achieved by it and in fact in obedience to provisions of such law as a measure of business expediency, there could be no valid reason not to allow such payment as deductible expenditure of the assessee under Section 37 of the Income Tax Act. [404H, 405-A, B]

**2.** Therefore, what needs to be done by an Assessing Authority under the Income Tax Act, 1961, in examining the claim of an assessee that the payment made by such assessee was a deductible expenditure under Section 37 of the Income Tax Act although called penalty, is to see whether the law or scheme under which the amount was paid required such payment to be made, as penalty or as something akin to penalty, that is imposed by way of punishment for breach or infraction of the law or the statutory scheme. If the amount so paid is found to be not a penalty or something akin to penalty due to the fact that the amount paid by the assessee was in exercise of the option conferred upon him under the very law or scheme concerned, to regard such payment as business expenditure of the assessee, allowable under Section 37 of the Income Tax Act, as an incident of business laid out and expended wholly and exclusively for the purposes of the business. However, such payment of the assessee is that which is made in exercise of the option given to such assessee by the law or the statutory scheme there arises no need for Assessing Authority to go into the question whether the payment could be regarded as that made as a measure of business ex-

A expediency, for it cannot ignore the fact in that, the law or the statutory scheme enables incurring of such expenditure in the course of assessee's business. [405-C to F]

3. The payments concerned were made in compliance with law or scheme concerned and not for committing any breach or infraction of the law or statutory scheme. Therefore, the judgment of the High Court is not liable to be interfered with. [405-G]

*Addl. Comm. of Income Tax, Gujarat v. Rustam Jehangir Vakil Mills Ltd.*, (1976) 103 I.T.R. 298 and *Commnr. of Income Tax Gujarat-III v. Tarun Commercial Mills Co. Ltd.*, (1977) 107 I.T.R. 172, approved.

C *M.S.P. Senthikumara Nadar & Sons v. Commn. of Income Tax*, (1957) 32 I.T.R. 138 Mad. and *Hazi Aziz and Abdul Shakoor Bros v. Commissioner of Income Tax*, (1961) 41 I.T.R. 350 S.C., held inapplicable.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 2123 of 1977 Etc. Etc.

From the Judgment and Order dated 18.11.1976 of the Gujarat High Court in Income Tax Reference Nos. 183, 125, 113, 33 and 164 of 1976.

E M.L. Verma, R. Salim, P.N. Misra, C. Ramesh & P. Parmeswaran for the Appellant.

A.K. Verma for JBD & Co. for the Respondent.

M.K. Puri for the Respondent in CAs. 726-731.

F The Judgment of the Court was delivered by

VENKATACHALA, J. These are the appeals of the Revenue arising from different judgments of the Gujarat High Court delivered on References, made at its instance under Section 256(1) of the Income Tax Act, 1961, to be referred to as 'the I.T. Act', on obtaining certificates of fitness to appeal to this Court. As the decision to be rendered by us in Civil Appeal No. 2149 (NT) of 1977 could form the basis for disposal of the remaining appeals, we shall proceed to consider that appeal and decide it at the first instance.

Civil Appeal No. 2149 (NT) of 1977 - *Commissioner of Income Tax, Gujarat v. Mihir Textiles Ltd.*

This appeal arises from the judgment in Income Tax Reference No. 175 of 1976 decided by the Gujarat High Court. The questions referred by the Tribunal under Section 256(1) of the I.T. Act for opinion of the High Court in that Reference, were these :-

1. Whether, the payment made to the Textile Commissioner by the assessee for contravention of the direction given by the Textile Commissioner was in the nature of penalty and not incidental to the carrying on of the assessee's business? A
2. Whether, on the facts and in the circumstances of the case, the payment of Rs. 1,70,766 made to the Textile Commissioner under the provisions of clause 21-C(1)(b) of the Cotton Textiles (Control) Order, 1948, as amended from time to time, was business expenditure allowable under Section 28 of the Income Tax Act, 1961 ? B
3. Whether, the payment of Rs. 5,17,781 made by the assessee to the Government for non-fulfilment of its obligation to export specified quantity of sanforized cloth is allowable as the payment incidental to carrying on of the assessee's business ? C

Facts which led to the reference of the said questions, for opinion of the High Court were briefly these :- D

A Textile Mill was being run by Mihir Textiles Ltd., Ahmedabad, the assessee, during the accounting year 1971-72 previous to the Assessment Year 1972-73. The assessee, being a manufacturer of cotton textiles, had to comply with the directions issued from time to time by the Textile Commissioner under the provisions of the Cotton Textiles (Control) Order, 1948, hereinafter referred to as 'the Control Order', as amended and then in force, in the matter of producing and packing minimum quantity of specified type of cloth by it during the accounting year. The assessee instead of producing and packing the minimum quantity of specified type of cloth as required by the aforesaid directions of the Textile Commissioner, paid to the Textile Commissioner Rs.1,70,766 in exercise of the option available to it under clause 21-C(1)(b) of the Control Order. Thereafter, when the assessee filed its income-tax return relating to the accounting year 1971-72 with the jurisdictional Income Tax Officer (ITO), it E

- A claimed deduction of the said amount out of its profits, as business expenditure. So also, the assessee, which had not fulfilled its export obligation under a bond entered into as regards exporting certain quantity of sanctioned cloth and paid to the Textile Commissioner Rs. 5,17,781 for non-fulfilment of that obligation, in exercise of its option available under the terms of the bond, claimed deduction of that amount as well in its income-tax return of the accounting year 1971-72 as its business expenditure. The I.T.O. who made the assessment order in respect of the said accounting year, refused to allow the claimed deductions, taking the view that the said amounts paid by the assessee to the Commissioner of Income Tax were not deductions which could be allowed as items of its business expenditure. In
- B appeal preferred by the assessee against that assessment order, the Appellate Assistant Commissioner, allowed the said amounts claimed by the assessee as items of its business expenditure in respect of its accounting year 1971-72 and made an order allowing the appeal. Revenue's appeal filed against that appellate order before the Tribunal did not meet with success. However, at the instance of the Revenue, the Tribunal referred the questions set out in the beginning of this Judgment for getting the opinion of the High Court on them.

and the Revenue did to no purpose as the Tribunal had already decided.

- A Division Bench of the High Court which examined the Reference, answered Questions 1 and 2 against the Revenue and in favour of the assessee following its earlier decision in *Additional Commissioner of Income-tax, Gujarat v. Rustam Jehangir Vakil Mills Ltd.*, (1976) 103 ITR 298. It also answered Question 3 against the Revenue and in favour of the assessee following its earlier decision in *Commissioner of Income-tax, Gujarat-III v. Tarun Commercial Mills Co. Ltd.*, (1977) 107 ITR 172. The
- F Reference was decided accordingly by the High Court by its judgment rendered in November 18, 1976. The Revenue, which was not satisfied with the said judgment of the High Court, has filed the present appeal in this Court on certificate of fitness obtained from the High Court to appeal to this Court.
- G It was not disputed before us that the answers given by the High Court in the *Rustam Jehangir Vakil Mills* case, if are sustainable, the answers given to Questions 1 and 2 by the High Court in the Judgment under the present appeal also become sustainable. So also, it was not disputed before us that the answers given by the High Court in *Tarun Commercial Mills* case followed in answering Question 3 in the Judgment
- H

under the present appeal, if are sustainable, the answer to Question 3 given by the High Court in the Judgment under appeal, as well, becomes sustainable. A

This situation leads us to the necessity of examining the correctness and the sustainability of the answers given by the High Court on the questions referred to it in References in *Rustam Jehangir Vakil Mills'* (Rustam Mills') Case and *Tarun Commercial Mills'* (Tarun Mills') case. B

The questions referred for opinion of the High Court in *Rustam Mills'* case (Income Tax Reference No. 14 of 1972), were :

1. Whether the payment made to the Textile Commissioner by the assessee for contravention of the direction given by the Textile Commissioner was in the nature of penalty and not incidental to the carrying on the assessee's business ? C
2. Whether on the facts and in the circumstances of the case the payment of Rs. 91,387 made to the Textile Commissioner under the provisions of clause 21-C(1)(b) of the Cotton Textiles (Control) Order, 1948 was business expenditure allowable under Section 28 or under Section 37 of the Act ? D

The High Court answered the above Question 1, thus : E

"The payment was not in the nature of panalty and was incidental to the carrying on of the assessee's business."

Then the High Court answered Question 2, thus : F

"The payment was business expenditure allowable under Section 37 of the Income Tax Act, 1961."

We shall advert here to the facts of *Rustam Mills'* case in order to examine the correctness and the sustainability of the answers given by the High Court to the questions referred thereto. For the assessment year 1969-70 the relevant accounting year being the financial year ending on March 31, 1969, the assessee-Mills failed to produce and pack the minimum quantity of the standard cloth required to be produced and packed according to a direction issued by the Textile Commissioner under the provisions of Cotton Textile (Control) Order, 1948. Rustam Mills which G H

- A had the option under clause 21-C(1)(b) of the Control Order, 1948 to pay to the Textile Commissioner, the amount envisaged thereunder in lieu of non-production and non-packing of the minimum quantity of the standard cloth in the year 1968-69, paid an amount of Rs. 91,387 to the Textile Commissioner. In the return of the Rustam Mills filed for the accounting year 1968-69, deduction of the amount of Rs. 91,387 was claimed as an allowance under Section 37 of the I.T. Act on account of its business expenditure of that year on the plea that it was an expense wholly and exclusively laid out for the purpose of its business. The Income Tax Officer refused to allow the deduction so claimed. However, in the appeal of the Rustam Mills, the Appellate Assistant Commissioner, allowed the deductions claimed and that order was confirmed by the Tribunal in the further appeal carried before it by the Revenue. In the Reference, carried before the High Court, at the instance of the Revenue, the aforesaid questions were answered against it by the High Court, as already stated. The answers so given to the questions by the High Court were based on its view that the amount paid by the Rustam Mills to the Textile Commissioner was neither penalty nor something akin to penalty paid for infraction of any law or public policy in as much as that amount was paid by Rustam Mills by exercising its option under clause 21-C(1)(b) of the Control Order, 1948; which formed part and parcel of a statutory scheme. Coming to *Tarun Mills'* case, the question referred for opinion of the High Court at the instance of the Revenue was :

- "Whether on the facts and in the circumstances of the case, penalty of Rs. 18,247 paid to the Textile Commissioner for non-fulfilment of the assessee's export obligation was business expenditure incurred wholly and exclusively for the purpose of the assessee's business."

- The High Court answered this question against the Revenue and in favour of Tarun Mills (the assessee). It would be necessary to advert to the facts of this case, in order to examine the correctness and the sustainability of the answer of the High Court given to the question. Tarun Mills became entitled to the user of trade mark 'Sanforized' on the authority given to it by the trade mark registry of the Government of India. that entitlement of Tarun Mills obligated it to export certain percentage of 'Sanforized' cloth produced by it. Accordingly, for the period from July, 1963 to November, 1965, Tarun Mills was required to export 5 per cent of the value of

'Sanforized' cloth produced by it, along with similar Mills which had become entitled to the user of the trade mark 'Sanforized'. But at the end of the year 1965, it was found that the required quantity of 'Sanforized' cloth was not exported by several Mills. So, a scheme was evolved by the Central Government to make the Mills concerned, to fulfil their export obligations. Under that scheme previous years' short-fall in the concerned Mills' exports was required to be made good by them during the subsequent years 1966 to 1972, besides the requirement on their part to export annually a quantity of not less than 10 per cent of the 'Sanforized' cloth produced during those years. The scheme also contained a provision requiring the concerned Mills to execute bonds in that regard in favour of the President of India. One of the conditions in that bond enabled the concerned Mills to pay to the Central Government 10 paise per linear yard on the shortfall in its export of 'Sanforized' cloth during the relevant year and that amount referred to as 'penalty' was required to be deposited with the Government of India.

Tarun Mills which did not export the required quantity of 'Sanforized' cloth during its accounting year 1967-68, made a deposit of Rs. 18,247 with the Central Government in exercise of its option under the bond to pay an amount in lieu of the shortfall in the quantity of 'Sanforized' cloth to be exported, and claimed that amount as its business expenditure in the Income-tax Return of the said accounting year. But, the Income Tax Officer refused to allow the said amount of deduction claimed as business expenditure of Tarun Mills during the relevant year. In appeal of Tarun Mills, the Appellate Assistant Commissioner reversed the order of I.T.O. and allowed deduction of that amount as its business expenditure. The Revenue's appeal therefrom filed before the Tribunals, did not succeed. At the instance of the Revenue, the question adverted to earlier, having been referred to the High Court, it was answered against the Revenue and in favour of the Tarun Mills, as stated earlier. In giving that answer, the High Court took the view that even if the bond referred to the amount payable by Tarun Mills for non-fulfilment of its export obligation as 'penalty' such amount being payable at the option of Tarun Mills for non-fulfilment of its export obligation under the scheme, it could not be regarded as penalty or something akin to penalty payable for any breach of law or public policy, for the very scheme under which that amount was payable by Tarun Mills to the Government, provided for such payment at the option of the concerned Mills.

A As the answers given by the High Court to the question referred for its opinion in *Rustam Mills'* case and in *Tarun Mills'* case have gone against the Revenue and in favour of the concerned assessee - Mills in view of the concerned scheme in the matter of payment of the amount to the Government of India, the points which require our consideration and decision in this appeal would be - whether the amount paid by the concerned Mills to the Government under the one or the other scheme becomes business expenditure of the Mills concerned, under Section 37 of the Income Tax Act as would entitle such Mills to claim deduction as its business expenditure for the accounting year.

B  
C Shri M.L. Verma, the learned Senior Counsel for the Revenue, contended that the amount paid by Rustam Mills in lieu of its failure to manufacture and pack the standard cloth during the accounting year 1967-68 as required under the scheme of the Control Order, 1948 has to be treated as the amount paid as penalty or as something akin to penalty for infraction of the law or public policy envisaged under the scheme and therefore, the said amount cannot be regarded as a business expenditure of the assessee - Rustam Mills under Section 37 of the Income Tax Act. He also contended that the amount which was claimed as deductible expenditure by Tarun Mills for non-fulfilment of its export obligation in relation to 'Sanforized' cloth had to be regarded as an amount paid by way of penalty or something akin to penalty for infraction of the law or public policy and hence could not be regarded as business expenditure claimable as deduction under Section 37 of the Income Tax Act. He sought to support his contentions placing reliance on the decisions of the Madras High Court in *M.S.P. Senthikumara Nadar & Sons v. Commissioner of Income-tax*, (1957) 32 I.T.R. 138 Mad., and of this Court in *Haji Aziz and Abdul Shakoor Bros. v. Commissioner of Income-tax*, (1961) 41 I.T.R. 350 S.C.

G In *Senthikumara Nadar's* case the assessee was doing business in coffee. It had entered into contracts with the Indian Coffee Board entitling it to purchase coffee on a rate far below the price of coffee sold within India, undertaking an obligation to export the whole of the coffee so purchased outside India. The assessee which purchased coffee at a low price because of the contracts, did not fulfil its export obligation by sending the whole of the coffee outside India. When the assessee was found to have committed the breach in performing his export obligation the assessee paid

liquidated damages to the Coffee Board as provided for in the terms of the contract. The assessee, thereupon, claimed that amount as deduction under Section 10(2)(xv) of the Income Tax Act, 1922. The Madras High Court which examined the nature of the payment made by the assessee found that that payment was akin to penalty, for it was paid for infraction of public policy underlying the Coffee Market Expansion Act, 1942, which was left to be enforced by the Coffee Board. That amount, it was found, was not an amount spent in the assessee's normal trading activity and not an amount paid as an incidental expenditure on account of business. In fact, this is what the High Court had to say in the matter : The breach of its contract here to the Board was not in the normal course of business, and the liability the assessee had to discharge for such breach was not incidental to the trading activities that it carried on. Hence, deduction of the said amount claimed by the assessee as business expenditure, was not accepted by the High Court.

In *Haji Aziz and Abdul Shakoor Bros.* case, this Court had to consider a situation where the assessee - Haji Aziz and Abdul Shakoor Bros. had imported certain goods in contravention of the law and the goods were on that account liable to be confiscated. However, the assessee obtained a release of the goods by paying a certain amount by way of fine. The question was whether the assessee could claim the amount so paid as fine as deductible business expenditure under Section 10(2)(xv) of the Income Tax Act, 1922. This Court, in that context, observed that a case involving payment of penalty for an infraction of the law fell outside the scope of permissible deductions under Section 10(2)(xv) of the Income Tax Act, 1922, by pointing out that the payment made by the assessee as liquidated damages was akin to penalty for an act of infraction of public policy underlying the concerned Statute. Hence, this Court held in that case that the amount paid by Haji Aziz and Abdul Shakoor Bros. as fine was not deductible as business expenditure under Section 10(2)(xv) of the I.T. Act.

We are unable to see, how any support could be derived from the said decisions for the contentions urged on behalf of the Revenue in this appeal.

In *Rustam Mills'* case, the concerned statutory scheme was found in certain clauses of the Cotton Textiles (Control) Order, 1948. Sub-clause (1) of clause 21A read thus :

- A "Where the Textile Commissioner has specified under paragraph (a) of sub-clause (1) of clause 22, the maximum prices at which any class or specification of cloth may be sold. .... he may, having regard to the matters specified in sub-clause (2) of clause 20, by order in writing direct any producer with a spinning plant or a group of such producers to pack such minimum quantity of such cloth and during such period as may be specified in the direction."
- B

- C Sub-clause (2) of clause 21A conferred power on the Textile Commissioner to grant extension of time for complying with the directions issued by him in so far as the price applicable to such quantities of cloth so packed is the price in force during the period specified in the direction under sub-clause (1) or during the extended period, whichever is lower.

Clause 21-C of that Order read :

- D "(1) Where the Textile Commissioner has issued directions under sub-clause (1) of clause 21A to any producer to pack a specified quantity of cloth during the period specified in the directions -

(a) .....

- E (b) such producer may, in lieu of packing the whole or part of the minimum quantity of cloth specified in the said direction, make payment to the Textile Commissioner in respect of the deficiency at such rates as may be specified by the Central Government and within such time as may be determined by the Textile Commissioner.
- F

(2) All payments received from producers under paragraph (a) of sub-clause (1) shall, as far as may be, be utilised towards payments, if any, to producers under the said paragraph (a)."

- G The Textile Commissioner's direction issued to the textile Mills to produce and pack a specified quantity of the standard cloth was in exercise of the powers conferred upon him under the said clauses. Rustam Mills instead of complying with the directions as to production and packing of required quantity of standard cloth availed of the option of making payment as provided under clause 21-C(1)(b) and paid to the Textile Commissioner a sum of Rs. 91,387. It is this amount which was claimed by
- H

Rustam Mills as deduction under Section 37 of the Income Tax Act, 1961 in respect of the relevant accounting year. The High Court found that amount to be deductible expenditure of the assessee-Rustam Mills. The statutory scheme contained in the said clauses was adverted to by the High Court thus :

"..... the scheme is that the law itself gives an option to the producer concerned to adopt one of the three courses and, if he complies with the law by choosing one of the three options offered to him, he cannot be said to commit any infraction of law. Hence, there is no question of any amount paid as penalty or any amount paid being akin to penalty as was the case before the Madras High Court in the Coffee Board case *Senthikumara Nadar & Sons v. Commissioner of Income- Tax*, (1957) 32 I.T.R. 138. ...."

Referring to the facts of the case, it was held by the High Court thus:

"In the instant case, the amount was spent by the manufacturer concerned for the purpose of carrying on its business and it was laid out and expended wholly and exclusively for the purposes of the business so that from the commercial point of view, he would carry on the business of manufacturing cotton cloth under the scheme set out in clauses 21A and 21C of the Cotton Textiles (Control) Order. Hence, the amount spent by the manufacturer would fall fairly and squarely within section 37(1) of the Income-tax Act, 1961 ....."

Turing now to *Tarun Mills'* case, the payment there, was made on account of non-fulfilment of the obligation of exporting 'Sanforized' cloth according to a term of the bond executed in favour of the President of India. The assessee - Tarun Mills paid the amount of Rs. 18,247 calculated at the rate of 10 paise per linear yard in lieu of shortfall in the export of 'Sanforized' cloth to be made by it as it was allowed, at its option, to do so, under another term of the bond. The contention advanced in that case on behalf of the Revenue was that the amount paid by Tarun Mills was an amount of penalty or an amount akin to penalty, for infraction of law or public policy and therefore, could not have been allowed as deduction of its business expenditure. On consideration of the matter, the High Court relied on *Rustam Mills'* case and held thus:

A "We are of the opinion that having regard to the terms contained  
in the bond we find that it is optional for the manufactures to  
achieve the export target prescribed for them or to pay to the  
Government the sum or sums calculated at the rate of 10 paise by  
linear yard to cover up the shortfall in the export obligations. The  
B option envisaged in the bond entered into between the parties  
clearly indicates that the option was with the manufacturers and  
that option may be availed of for a variety of reasons in the interest  
of commercial expediency. The export obligations which the textile  
C manufacturers may have incurred for the use of trade mark  
'sanforized' may not be fulfilled for various factors over which the  
manufacturers may not have control. The trend and competition  
in the international market, the quality and quantity of the goods  
produced by the manufacturers may be some of the factors which  
may ultimately have a bearing on the question of achieving the  
target. In the interest of business, textile manufacturers opt for  
D payment of compensation or damages to cover up the shortfall in  
the export obligations. It is no doubt true that the word used in  
the scheme which we have set out above for the sum to be paid in  
default of fulfilling the export obligation has been described as a  
penalty but in the ultimate analysis it is the substance of the  
transaction between the parties which has to be considered for  
E purposes of determining what is the nature and import of the  
scheme and the bond executed in pursuance thereof. The exercise  
of option, as stated above, may be the result of the commercial  
expediency as well as certain extraneous factors over which the  
F manufacturers might not have the control and, therefore, in view  
of the scheme and the bond with which we are concerned here, it  
cannot be said that there is a breach of a public policy which may  
render the payment, agreed to be made for the default arising as  
a result of the breach, as one akin to penalty. Under no circumstan-  
ces, without violence to the language, it can be said to be infraction  
G of the law."

It is ture, that a payment made by an assessee doing business in the  
accounting year is not entitled to claim deduction under Section 37 of the  
I.T. Act, 1961 of an amount paid by such assessee during the year as an  
amount of penalty or an amount akin to penalty for any breach or infraction  
H of law or any public policy which is sought to be achieved by such law, as

is also held by this Court in *Haji Aziz and Abdul Shakoor Bros.*' case. But if such payment is made by the assessee during the relevant accounting year without any breach or infraction of any law or any public policy sought to be achieved by it and in fact in obedience to provisions of such law as a measure of business expediency, there could be no valid reason not to allow such payment as deductible expenditure of the assessee under Section 37 of the I.T. Act.

Therefore, what need to be done by an assessing Authority under the I.T. Act, 1961, in examining the claim of an assessee that the payment made by such assessee was a deductible expenditure under Section 37 of the I.T. Act although called penalty is, to see whether the law or scheme under which the amount was paid required such payment to be made, as penalty or as something akin to penalty, that is imposed by way of punishment for breach or infraction of the law or the statutory scheme. If the amount so paid is found to be not a penalty or something akin to penalty due to the fact that the amount paid by the assessee was in exercise of the option conferred upon him under the very law or scheme concerned the assessing Authority has to regard such payment as business expenditure of the assessee, allowable under Section 37 of the I.T. Act, as an incident of business laid out and expended wholly and exclusively for the purposes of the business. However, if such payment of the assessee is that which is made in exercise of the option given to such assessee by the law or the statutory scheme there arises no need for Assessing Authority to go into the question whether the payment could be regarded as that made as a measure of business expediency, for it cannot ignore that fact in that, the law or the statutory scheme enables incurring of such expenditure in the course of assessee's business.

As is pointed out by us already, the High Court has answered the questions referred to in *Rustam Mills'* case as well as in *Tarun Mills'* case, taking into consideration the facts that the payments concerned therein were made in compliance with law or scheme concerned therein and not for committing any breach or infraction of the law or statutory scheme. Therefore, the judgment of the High Court under the present appeal being rendered following its earlier judgments *Rustam Mills'* case the *Tarun Mills'* case, which are found by us to have been rendered in consonance with law, the same is not liable to be interfered with.

In the result, we dismiss the Civil Appeal No. 2149 (NT) of 1977,

A with no costs.

CIVIL APPEAL NOS. 2123, 2171-72, 2226, 2241 AND 2243 OF 1977.

As our Judgment in the above Civil Appeal No. 2149 (NT) of 1977 fully covers the subject matter of these appeals, they are liable to be

B dismissed, following that Judgment.

In the result, we dismiss these Appeals, as well, with no costs.

T.N.A.

Appeals dismissed.