

Shahzada Nand & Sons v. Commissioner of Income Tax, Patiala

Civil Appeal No. 1011 of 1972

[1977] 3 SCR 529 | 1977-04-12

Whether genuine commission paid to two long-serving employees was deductible under the historical section 36(1)(ii) despite no proof of extra services over earlier years, and how reasonableness should be assessed under its then proviso.

36(1)(ii) (text applicable to AY 1963-64)

3-judge bench | P.N. Bhagwati, J. | N.L. Untwalia, J. | S. Murtaza Fazal Ali, J.

Assessment years: 1963-64

Historical employee-commission provision; no automatic deduction

For AY 1963-64, genuine Rs.45,380 commission for actual services was allowed without an extra-services or contractual-obligation prerequisite. The old reasonableness proviso, the profit/dividend restriction and all the proved circumstances matter; the 2011 version separately checked does not reproduce that old proviso. This is not a universal partner-payment or voluntary-bonus rule. Reported turnover/rate figures are not silently reconciled. Costs cover both appeal and reference. Comprehensive later treatment, current law and 2025 mapping are not verified.

01 FACTS OF THE CASE

The registered firm was sole selling agent for yarn, cloth and blankets of Oriental Carpet Manufacturers India Pvt. Ltd. (OCM). Of the five partners, only Madan Lal attended day-to-day management; he was assisted by Saheb Dayal and Gurditta Mal as employees. The body also lists Saheb Dayal as a partner representing a trust, and identifies family relationships of two other partners. The employees had long attended to the business, received Rs.1,000 monthly salary each and, in the disputed year, bonus equal to three months' salary each (physical pages 2-3/SCR 530 G-531 B; page 5/SCR 533 E-H).

For AY 1963-64 the source reports turnover of Rs.54.28 lakh, overriding commission from OCM of Rs.1,13,449 and total profit of Rs.3,08,034. The firm paid each employee Rs.22,690 additional commission, Rs.45,380 in total. It considered them principally responsible for the business's prosperity. The Court's stated money figures are retained; the printed rate-and-turnover recitals are not used to recompute the operative deduction (physical page 3/SCR 531 C-G; page 8/SCR 536 A-D).

The assessing officer, appellate authorities and High Court rejected the commission claim for want of proof of extra services justifying it. Salary and bonus had initially also been rejected by the officer but were allowed by the first appellate authority. The genuineness of the commission payment itself was never in dispute. The firm brought this special-leave appeal from the Punjab and Haryana High Court's answer to the reference (physical pages 2, 4-5/SCR 530 F, 532 A-H and 533 A-H).

Source: See the proposition-specific paragraph and PDF-page references below.

02 DISCUSSION BY THE HON'BLE COURT

The Court reproduced section 36(1)(ii) as it stood for AY 1963-64: employee bonus or commission must be for services rendered and must not be a sum otherwise payable as profit or dividend; the then proviso called for reasonableness by reference to pay/service conditions, business profits and practice in similar businesses. The judgment does not set aside those statutory requirements (physical page 5/SCR 533 A–E).

Services were actually rendered. The statute did not require additional or more onerous services than in earlier years and did not insist on a contractual obligation to pay commission. Voluntary payment could qualify. Absence of extra services was still a relevant circumstance in testing reasonableness, but not an automatic disqualification. The three proviso factors were considerations rather than rigid cumulative conditions; reasonableness was judged from a normal prudent businessperson's standpoint and commercial expediency, not the officer's subjective standard (physical pages 6–7/SCR 534 A–535 F).

On these facts the established employees' contribution, growth in turnover and overriding commission, remuneration and total profit justified Rs.45,380. The Court's discussion of employee incentives, profit-sharing and social justice supported that commercial conclusion. It was not a separate command to deduct every voluntary payment or to distribute profits. A sham payment or no services would not qualify. No general section 40(b) partner-remuneration issue was formulated or adjudicated (physical pages 5–9/SCR 533 A–B, 534 E–H and 535 G–537 B).

Source: See the proposition-specific paragraph and PDF-page references below.

03 JUDICIAL DECISION

The Rs.45,380 employee commission was held reasonable on all the circumstances and deductible under the historical section 36(1)(ii). The appeal was allowed, the High Court's judgment set aside and the referred question answered affirmatively for the assessee. The Commissioner was ordered to pay the assessee's costs of both the appeal and the reference (physical page 9/SCR 537 B–C).

Source: See the proposition-specific paragraph and PDF-page references below.

04 OUTCOME / IN WHOSE FAVOUR

In whose favour: Assessee firm

Appeal allowed; High Court judgment set aside; Rs.45,380 deduction affirmed; Commissioner to pay appeal and reference costs

Final substantive construction and fact-specific application of section 36(1)(ii) as applicable to AY 1963-64

Genuine payment for actual services and historical statutory limitations remain. No extra-service or contractual-payment prerequisite, but no universal deduction of every voluntary bonus or commission. The old proviso must not be represented as unchanged later text.

Source: See the proposition-specific paragraph and PDF-page references below.

05 AKHB REVIEW POINT

Ask whether services were genuinely rendered and why the payment was commercially reasonable, rather than imposing an extra-services condition which the Court found absent from the historical provision. Existing salary and bonus did not automatically exhaust the employer's permissible response to a successful year.

Retain the full statutory setting and employee capacities. The trust-representative partner recital does not establish a universal rule for payments to partners. A separately checked 2011 statutory text retains the profit/dividend restriction but does not reproduce the old reasonableness proviso. That comparison illustrates why historical reasoning cannot substitute for checking the particular later year's deduction, disallowance and timing rules.

Source: See the proposition-specific paragraph and PDF-page references below.

PROPOSITION-SPECIFIC SOURCE PARAGRAPHS AND PDF PAGES

1.

Topic: Date, bench, docket, partners and employees

Source url: [Open cited source](#)

Pdf pages: 1; 2; 3

Paragraphs: SCR 529 heading; 530 F-531 B

Source role: reported metadata and judicial text

2.

Topic: Comparative business figures and exact commission

Source url: [Open cited source](#)

Pdf pages: 3

Paragraphs: SCR 531 C-H

Source role: judicial text

3.

Topic: Lower decisions and referred question

Source url: [Open cited source](#)

Pdf pages: 4

Paragraphs: SCR 532 A-H

Source role: judicial text

4.

Topic: Genuine payment and complete historical statutory text

Source url: [Open cited source](#)

Pdf pages: 5

Paragraphs: SCR 533 A-H

Source role: judicial text

5.

Topic: Actual versus extra services and contractual obligation

Source url: [Open cited source](#)

Pdf pages: 6; 7

Paragraphs: SCR 534 A–535 B

Source role: judicial text

6.

Topic: Proviso factors and prudent businessperson standard

Source url: [Open cited source](#)

Pdf pages: 7

Paragraphs: SCR 535 C–H

Source role: judicial text

7.

Topic: Commercial application, final sum and both costs awards

Source url: [Open cited source](#)

Pdf pages: 8; 9

Paragraphs: SCR 536 A–537 C

Source role: judicial text

8.

Topic: Separately labelled Act commencement and complete savings check

Source url: [Open cited source](#)

Pdf pages: 42; 1004; 1005; 1006

Paragraphs: Printed 1.1 and 1.963–1.965; full sections 1 and 297; scope corroboration only

Source role: official hosted statutory compilation bounded check

9.

Topic: Separate later-version comparison of commission clause

Source url: [Open cited source](#)

Pdf pages: 278; 279

Paragraphs: Printed 1.237–1.238; section 36(1) opening and complete clause (ii); commentary footnotes separately labelled

Source role: official hosted statutory compilation bounded check

JUDICIAL AUTHORSHIP AND SEPARATE OPINIONS

P.N. Bhagwati, J.

ACT IDENTIFIED IN THE REVIEWED SOURCE

Income-tax Act, 1961 (historical section 36(1)(ii); Act identity separately corroborated by commencement/savings and statutory text)

OTHER STATUTORY PROVISIONS AND THEIR SEPARATE SCOPE

Income-tax Act, 1961, sections 1 and 297: separately checked for historical Act scope, not sections applied or adjudicated by the Court in this judgment.

SPECIFIED LATER JUDICIAL OR STATUTORY CHECKS AND THEIR LIMITS

1.

Kind: historical scope crosscheck not court reasoning

Status: bounded verified

Source urls: [https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=42;](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=42)
[https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=1004;](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=1004)
[https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=1005;](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=1005)
[https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=1006;](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=1006)
[https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=279](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=279)

Finding: The 1961 Act commenced 1 April 1962 subject to its provisions; section 297's relevant earlier-assessment/pending-proceeding savings do not describe this original AY 1963-64 commission assessment. The exact section 36(1)(ii) opening is corroborated in the official-hosted compilation. Earlier turnover figures are background, not old-Act appeals.

Limit: An editorial inference from the actual AY, proceeding and statutory text, separately labelled. It does not assert that the Court invoked sections 1 or 297.

2.

Kind: later statutory version comparison

Status: bounded verified

Source urls: [https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=278;](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=278)
[https://dor.gov.in/files/acts_files/IT%20Act%20\(English\)_0.pdf#page=279](https://dor.gov.in/files/acts_files/IT%20Act%20(English)_0.pdf#page=279)

Finding: The 2011 reproduced section 36(1)(ii) retains actual-services and profit/dividend language but not the old proviso quoted at SCR 533.

Limit: Complete clause (ii) and section 36(1) opening read; no other clause/current disallowance regime or authenticated Gazette amendment chain claimed.

SOURCE & VERIFICATION

Hon'ble Supreme Court source PDF (reported judgment)

Identified source rendition: 9 PDF pages; SHA-256

1096d9456656f51c2a68b58da159c9093478f23ea1e625c24f34d312619f784b. Original bytes preserved.

Judicial body begins physical page 2/SCR 530 G and ends physical page 9/SCR 537 C. Page 1 and page 2 through E contain reporter summary; page 2 F contains appellate metadata. No neighbouring judgment.

Open cited source rendition

The body repeatedly quotes and decides section 36(1)(ii) for AY 1963-64 but does not spell out the Act's year. A separately labelled sections 1/297 and reproduced section 36 check establishes the 1961 Act context; those checks are not attributed to the Court.; AYs 1960-61, 1961-62 and 1962-63 supply business history only. Only AY 1963-64 is decided.; The source reports Rs.54.28 lakh turnover, overriding commission Rs.1,13,449 and commission Rs.22,690 each; its rate recitals do not arithmetically reconcile directly with the reported turnover. The awarded Rs.45,380 is clear and is not recomputed.; Saheb Dayal's trust-representative partnership capacity is stated in the facts, but the decided issue concerns genuine employee commission under section 36(1)(ii), not a formulated section 40(b) dispute.; The operative order awards costs of both appeal and reference.; The historical reasonableness proviso differs from the separately reviewed 2011 text. Editorial amendment-history footnotes are not treated as authenticated enacted amendments.

Only AY 1963-64 is adjudicated. Figures for AYs 1960-61 to 1962-63 are comparison history, not additional assessment appeals.

STATUTORY SCOPE

No automatic mapping to the Income-tax Act, 2025 and no present-law certification. Verify the applicable statutory version and procedural route separately.

LATER TREATMENT

Source checked 2026-10-05. not_verified. Bounded statutory comparison only: the official Department of Revenue-hosted 2011 compilation, physical pages 278–279, was read for the section 36(1) opening and complete clause (ii). The provision retains the services and profit/dividend restrictions but no longer reproduces the old reasonableness proviso. Publisher footnotes describe later amendments; no original Gazette-chain finding or current-year tax treatment is certified. Sections 1 and 297 were independently read only to corroborate historical scope, not as later judicial treatment. No comprehensive citator or 2025 mapping.

IDENTIFIED SOURCE LINKS

[reported judgment - PDF pages: 9](#)

SHA-256: 1096d9456656f51c2a68b58da159c9093478f23ea1e625c24f34d312619f784b

[official hosted statutory compilation - PDF pages: 1251](#)

SHA-256: 1ec6e4c38dc1d524d1d40b1fd35d13ac1336c8fc549cef2af1bf723a999c822b

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