THE EMPLOYERS OF AZAM JAHI MILLS LTD.

v.

THE WORKMEN

(*January* 30, 1967)

[M. HIDAYATULLAH, V. BHARGAVA AND G. K. MITTER, JJ.]

Industrial Dispute—Bonus agreed to be paid only on available surplus —calculation of surplus—Whether gratuity and retrenchment compensation to be deducted in one year or spread over more—Whether deduction of amount in respect of idle machinery from notional amount of normal depreciation justified—Rehabilitation charges—Nature of evidence required to justify deduction.

The appellants and their workmen had entered into an agreement in February 1960 which provided that a claim for bonus would only arise if there should be an available surplus after making a provision for all the prior charges including a fair return on paid up capital and on reserves utilised towards the working capital in terms of the Full Bench formula

In a dispute between the appellants and their workmen relating to the payment of bonus for the years 1960-61 and 1961-62, the Industrial Tribunal found that there was an available surplus for the first year but none for the second, and therefore directed payment of bonus of one week's wages to all the workmen over and above the two weeks' bonus which the employees had agreed to pay irrespective of any profits made by the company.

In the appeal before this Court it was contended, *inter alia*, on behalf of the appellants that in the calculation of the gross profits, the entire amount in respect of gratuity and retrenchment paid by the company during the year 1960-61 should have been excluded as it had to be paid out of the profits of the company during the relevant year and the Tribunal had wrongly decided that it should be spread over five years; that in calculating prior charges, the Tribunal had wrongly deducted a sum of Rs. 1.50 lakhs in respect of idle machinery from the figure of notional normal depreciation and some of the other prior charges were not dealt with in accordance with the terms of the agreement between the parties; and that if calculations were made on a correct basis there would be no available surplus.

HELD : On a recalculation of the gross profits and prior charges, that the Tribunal was not right in finding that there was an available surplus for calculation of bonus for the year 1960-61. [527 A-B]

Gratuity would have to be paid year after year to workmen who retire or leave the company's service in terms of the scheme of gratuity and retrenchment compensation may have to be paid in any year if there be modernisation of the plant or for any other reason which renders any workmen surplus. The Tribunal's decision that the amount on this account should be spread over five years was therefore erroneous and the gross profit as calculated by the appellants was the correct figure. [523 A-C]

Britannia Engineering Co. v. *Their Workmen* [1965] II L.L.J. 144; referred to.

The depreciation taken into account being, in accordance with well settled principles, a notional amount of normal depreciation, the Tribunal was not justified in deducting therefrom a further sum in respect of idle machiner. [523 H; 524 C-D]

A *U.P. Electric Supply Co. Ltd.* v. *Their Workmen* [1955] II L.L.J. 431; *Surat Electricity Company's Staff Union* v. *Surat Electricity Co. Ltd.* [1957] II L.L.J. 648; *The Associated Cement Companies Ltd.* v. *Its Workmen* [1959] S.C.R. 925, 960; referred to.

On the facts, there was sufficient evidence to show the need for rehabilitation and there was no force in the contention that there was no basis for calculation of the provision for rehabilitation because no experts were B examined before the Tribunal. [526 C]

M/s Peirce Leslie & Co. Ltd. Kozhikode v. *Their Workmen* [1960] 3 S.C.R. 194 *Aluminium Corporation of India, Ltd.* v. *Their Workmen*, [1963]—II L.L.J. 629, distinguished.

CIVIL APPELLATE JURISDICTION : Civil Appeals Nos. 971 and 972 of 1965.

C Appeals by special leave from the Award dated December 21, 1963 of the Industrial Tribunal, Andhra Pradesh, Hyderabad in Industrial Dispute No. 28 of 1963.

A. K. Sen, R. V. Pillai and *B. K. Seshu*, for the appellant (in C.A. No. 971 of 1965) and the respondent (in C.A. No. 972 of 1965)

M. K. Ramamurthi, for the respondent (in C.A. No. 971 of D 1965) and the appellant (in C.A. No. 972 of 1965).

The Judgment of the Court was delivered by

Mitter, J. This is an appeal against an award dated December 21, 1963 in Industrial Dispute No. 28 of 1963 of the Industrial Tribunal, Andhra Pradesh, Hyderabad on special leave granted by E this Court.

The dispute which was referred to the Industrial Tribunal related to the question of payment of bonus for the years 1960-61 and 1961-62 demanded by the workers of Azam Jahi Mills, Warrangal. The Tribunal found that there was an available surplus for the first year but none for the second. It directed payment of bonus F of one week's wages to all the workmen over and above the two weeks' bonus which the employers had agreed to pay irrespective of any profits made by the company. In appeal before us the appellants contend that as there was no available surplus, if properly quantified, the question of payment of bonus in addition to that for the two weeks already agreed upon, does not arise. It is to be noted that the parties had entered into a settlement on February 22, G 1960 which was to be operative for a period of five years commencing on October 1, 1958 and ending on September 30, 1963. By that settlement, it was provided that the claim for bonus would only arise if there should be an available surplus after making a provision for all the prior charges including a fair return on paid-up capital and on reserves utilised towards the working capital in terms of the H Full Bench formula laid down by the Labour Appellate Tribunal in *Millowners' Association* v. *Rashtriya Mills Mazdoor Sangh, Bombay*. The agreement also provided that prior charges would include (a) statutory depreciation and development rebate, (b) taxes, (c

reserve for rehabilitation, replacement and modernisation of Block as calculated by the Industrial Court (basic year 1947) and (d) a fair return at 6% on paid up capital in cash or otherwise including bonus shares and 2% on reserves employed as working capital. It was also a term of the agreement that the amount of the total gross profits of the mill for the year shall be the amount of profits as disclosed in published balance sheets of the company without making a provision for depreciation and for bonus, but after deducting from it the amount of extraneous income (like interest from investments, rent from property) which is unrelated to the efforts of the workers. With regard to statutory depreciation and development rebate, the parties agreed that if in any year the total of these two exceed the amount of reserve for rehabilitation, the full amount of statutory depreciation and development rebate would be adopted as a prior charge and no extra provision would be made for rehabilitation in that year. Further, in terms of the agreement, the workers would be entitled to an amount equivalent to 1/24th of the basic wages if the mill had an available surplus of profits after providing for all prior charges on the basis of the Full Bench formula as described above, up to an amount equivalent to 25% of the total basic wages earned during the year.

The contention of the appellants before us is that in working out the available surplus the Tribunal went beyond the Full Bench formula and the settlement between the parties. Our task was considerably lightened by counsel for the appellants handing over a table showing the figures for the working out of the Full Bench formula, as found by the Tribunal compared to those propounded by the Management and the workers. There is no dispute that the net profits as disclosed by the balance sheet for the year 1960-61 was Rs. 9,03,378/-. The only difference between the management and the Tribunal with regard to the calculation of gross profits relates to the figure Rs. 5,39,963/- for gratuity and retrenchment compensation paid by the company during the year in question. According to the Tribunal, this sum should be spread over five years while according to the company, this sum should not be included at all as it had to be paid out of the profits of the company during the relevant year.

Mr. Sen, counsel for the appellants, relied on s. 37(1) of the Income-tax Act, 1961 for the purpose of showing that any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the pupose of the business or profession of the assessee has to be allowed in computing the income chargeable under the head 'profits and gains of business or profession'. He argued that gratuity is to be paid every year to the workmen who retire and retrenchment compensation has to be paid as and when workmen are retrenched and that there could be little doubt that

A these expenses were incurred exclusively for the purpose of the business of the company. He also drew our attention to a judgment of this Court in *Britannia Engineering Co.* v. *Their Workmen*(1) where it was laid down that the amount of provident fund contribution and gratuity payments were not to be added back to the net profits disclosed by the balance sheet of the company for fixing B the amount of gross profits in working out the Full Bench formula. The Tribunal apparently recognised the force of the contention of the employers but observed that the amount should be distributed over a number of years which it fixed as five in this case. This finding of the Tribunal is erroneous inasmuch as gratuity will have to be paid year after year to workmen who retire or leave the company's C services in terms of the scheme of gratuity and retrenchment compensation may have to be paid in any year if there be modernisation of the plant, or for any other reason which renders any workmen superfluous. It seems to us, therefore, that the gross profits as calculated by the employers at Rs. 19,05,496/- is the correct figure.

Coming next to the ascertainment of prior charges, the material D discrepancy between the figures adopted by the company and those by the Tribunal arises thus—we find that the notional normal depreciation has been taken to be Rs. 6,44,351/- in both sets of charts but the Tribunal has deducted therefrom a sum of Rs. 1,50,000/- in respect of idle machinery. We are unable to accept this view of the Tribunal. It is well settled that depreciation allowed under the Income-tax Act after 1948 was to consist of the statutory normal E depreciation as well as initial depreciation and additional depreciation. The Full Bench formula of the Labour Appellate Tribunal decided in *U.P. Electric Supply Co. Ltd.* v. *Their Workmen*(2) that the depreciation which should be deducted from the gross profits in working the formula was normal depreciation including the multiple shift depreciation but excluding the initial depreciation and F additional depreciation allowable under the Income-tax Act. This decision was followed by another Labour Appellate Tribunal of India in *Surat Electricity Company's Staff Union* v. *Surat Electricity Co. Ltd.*(3). There it was pointed out that the deduction allowed under the head of depreciation in the early years of the use of the machinery was rather heavy under the provisions of the G Indian Income-tax Act which would have the effect of unduly lessening the available surplus under the bonus formula to the prejudice of workers even in a year of prosperity and that is why the Full Bench postulated for a more even distribution of depreciation over a period of years. This accounted for the ignoring of the initial and additional depreciation in working out the bonus formula. The net result was that the depreciation to be taken into account for H working out the bonus formula was a notional amount of normal

(1) [1965] II L.L.J. 144. (2) [1955] II L.L.J. 431.

(3) [1957] II L.L.J. 648.

depreciation. No objection can be taken to this because the bonus formula itself is theoretical one. Both these decisions were referred to in *The Associated Cement Companies Ltd.* v. *Its Workmen*(1), and the latter decision was approved of by this Court (see at page 960).

We find by referring to Schedule E of the accounts of the company for the year 1960-61 that depreciation for the year was calculated at Rs. 16,03,149/-. This is also referred to in the Director's Report. Deducting therefrom the sum of Rs. 9,58,798/- which is referred to in the profit and loss account for the year ended 30th September 1961 as balance provision for depreciation to comply with s. 205 of the Companies Act of 1956, we get the figure of Rs. 6,44,351/- which is to be found in the chart both under the table of figures adopted by the management as also by the Tribunal. The figure being a notional figure for working out the bonus formula, the Tribunal was not justified in deducting therefrom a further sum of Rs. 1,50,000/- in respect of machinery which was said to be idle.

In terms of the agreement between the parties, the prior charges must include the development rebate as well unless the statutory depreciation and development rebate added up to a higher figure than the figure for reserve and rehabilitation. It therefore appears to us that the Tribunal was not justified in excluding the amount of the development rebate reserve. There is no dispute that the figure for income-tax should be Rs. 4,74,020/- or that for the return on paid-up capital should be Rs. 4,32,000/-. The workmen in their chart have calculated the return at 4% on Rs. 72 lakhs which is not justified. Both the Tribunal and the company calculated return on reserves used as working capital at Rs. 49,678/-. This, in our view, is not justified as we find from a reference to schedule E, (fixed assets of the company for the year 1960-61) that a sum of Rs. 14,49,664/- was spent for addition of new plant and machinery. On a reference to schedules A, B, C and D for the year in question and the corresponding figures for the previous year, we find that the figure of reserves and surplus in schedule A has gone down by Rs. 1,00,000/-. The figure for secured loans in schedule C remains the same while the current liabilities as shown in schedule D has gone up by Rs. 3,50,000/- in the year in question as compared to the previous year and loans secured from banks show a reduction of Rs. 13,22,000/-. Thus the liability in respect of the loans has been reduced approximetely by Rs. 10 lakhs. Setting off the diminution the overall liability was diminished by Rs. 9 lakhs. We also find from a reference to Schedules F, G, H and I (of investments, current assets and loans by the company) that the total thereof has gone down by Rs. 8 lakhs from the figure of the previous year. The net

(1) [1959] S. C. R. 925.

A result seems to be that the reduction of liability when set off against the reduction in the value of the assets and investments gives a deficit of Rs. 1,00,000/- approximately. As the company has not incurred any fresh loans for the purpose of buying plant and machinery we can proceed on the basis that Rs. 14,49,664/- and Rs. 1 lakh have come out of the working capital. Consequently, the reserves used as
B working capital should be approximately Rs. 24,83,000/- as shown by the company less Rs. 15,49,664/- *i.e.* Rs. 8,34,000/- and the return thereon at 2% would be approximately Rs. 16,000/- in place of Rs. 49,678/-. Further, we find that the Tribunal was not right in including Rs. 1,07,992/- as gratuity and retrenchment compensation among its list of prior charges.

C On the basis of the above, it seems to us that deducting the prior charges from the gross profits irrespective of the question of the amount to be deducted for rehabilitation, modernization etc., comes to the figure arrived at is Rs. 80,000/- or there about only.

There was a good deal of controversy between the parties with regard to the correct amount of the figure for rehabilitation. In
D this connection, our attention was drawn to the evidence on record. The Chief Engineer of the Company stated before the Tribunal that the machinery had been purchased in 1932, that its condition was bad due to fatigue and that it was costing more and more every year for repairs even up to Rs. 2½ lakhs. According to him, it required replacement, the average life of a textile mill being no
E more than 25 years. The witness also said that one half of the entire machinery had been purchased and installed between 1948 and 1952 and the cost in 1952 was five times that of the 1932 figure. The other witness examined on behalf of the employers was the Secretary of the mill. He stated that the provision for rehabilitation was Rs. 93,30,000/-, the working capital being Rs. 24,83,904/-. He gave certain figures to show how the figure of Rs. 93,30,000/-
F was arrived at. He stated further that the company had approached the Government for a loan of Rs. 56 lakhs for replacement of the spinning machinery and part of the weaving machines. The application for loan is not in dispute before us. As a matter of fact, the Tribunal accepted the evidence that the age of the textile mill machinery was about 25 years and more than half the
G machinery had passed that age. This justified the need for rehabilitation. The Tribunal referred to a letter of the company to the Government dated October 10, 1963 according to which several experts had opined that the amount required for replacement of the old machinery was Rs. 56 lakhs. The Tribunal added thereto the sum of Rs. 2 lakhs for replacement
H of the buildings and thus arrived at the total figure of rehabilitation of Rs. 58 lakhs. In our opinion, the figures arrived at by the Tribunal are acceptable but we have to deduct therefrom the amount of the reserves of the company. According to us, as already shown,

the reserves which could be used as working capital were no more than Rs. 8,34,000/-. Thus the total for rehabilitation comes to Rs. 50 lakhs approximately. The Tribunal accepted the divisior 5 to give effect to the bonus formula on the basis that the cost of rehabilitation should be spread over five years. In our opinion, the Tribunal proceeded on the right basis except on the figure of reserves which has to be deducted. Dividing Rs. 50 lakhs by five, we get a figure of Rs. 10 lakhs. In terms of the bonus formula therefore, there was no available surplus for the year 1960-61 but there was a deficit.

We were not impressed by the argument on behalf of the respondents that as no experts were examined before the Tribunal, there was no basis for calculation of the provison for rehabilitation. In this connection our attention was drawn to a judgment of this Court in *M/s Peirce Leslie Co. Ltd. Kohzikode* v. *Their Workmen* (1). It appears that in support of its claim in that case the company produced a number of statements prepared by witnesses who claimed to be experts showing the replacement value of buildings, machinery, furniture etc. We were also referred to the judgment of this Court in *Aluminium Corporation of India, Ltd.* v. *Their Workmen*(2). On the facts of that case, it was observed by this Court that as there was no evidence adduced by the employer to substantiate its claim for the amount of rehabilitation, the same must be rejected. In our view, the Tribunal must consider all the evidence before it and then proceed to ascertain the figure to be adopted for rehabilitation purposes. If the company had no scheme for rehabilitation, then of course its claim on that head must be rejected. Again, the claim made by the company cannot be accepted unless substantiated by evidence. In this case, we find that half the machinery was over 25 years old, that it required over Rs. 2 lakhs every year for repairs according to the evidence of the Chief Engineer and that its efficiency had dwindled considerably. We also see no reason to reject the evidence adduced before the Tribunal that the company had applied for a loan of Rs. 56 lakhs from the Government for rebabilitation purposes and we accordingly are of the view that the Tribunal proceeded on the correct basis so far as rehabilitation charges are concerned.

There remains the point about the working capital of the company. No case is here made that the reserves of the company were being used for any purpose other than the business of the company. The accounts of the company show that its secured liability exceeded Rs. 1,16,00,000/- and its unsecured loans exceed Rs. 28,00,000/-. Unless therefore there is evidence to show that the reserves were non-existent or they were being utilised for a purpose other than

(1) [1960]3 S.C.R. 194. (2) [1963] II L.L.J. 629.

A the business of the company, it is reasonable to assume that the reserves were being utilised as working capital of the company.

In our view, therefore, the Tribunal was not right in finding that there was available surplus for calculation of bonus for the year 1960-61 and the appeal No. 971 of 1965 must be allowed and the award set aside.

B

The other appeal No. 972 of 1965 which is by the workmen for enhancement of the bonus consequently must be dismissed. The first appeal is therefore allowed with costs and the second appeal is dismissed, but, without any order as to costs.

R.K.P.S.

Appeal 972 *of* '65 *dismissed*.
Appeal 971 *of* '65 *allowed*.