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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ W.P.(C) 17018/2024

SAILESH H MEHTA .....Petitioner

Through: Mr Aditya Bharat Manubarwala with Mr Kalash Pandey, Ms Akriti Manubarwala, Ms Tanishka Grover and Mr Naman Maheshwari, Advocates.

versus

UNION OF INDIA & ORS. .....Respondents

Through: Mr Puneet Rai with Mr Ashvini Kumar and Mr Rishabh Nangia, Advocates for R2.
Mr Kamal Mehta with Mr Akul Mehandru, Advocates for R3.

CORAM:
HON'BLE THE ACTING CHIEF JUSTICE
HON'BLE MR. JUSTICE TUSHAR RAO GEDELA

O R D E R

% **09.12.2024**

1. The petitioner is an individual and has filed the present petition *inter alia* impugning the constitutional validity of Rule 102 of the Income Tax Rules, 1961 as violative of Articles 14 and 21 of the Constitution of India insofar as it denies admission of directors holding more than 5% voting shares to the gratuity fund. In addition, the petitioner also prays that directions be issued to the respondents to extend gratuity benefits to the petitioner under LIC Gratuity Fund Scheme as is applicable to other employees.

2. The petitioner claims that the petitioner is a promoter of a company

known as Duflon Industries Pvt. Ltd. (hereafter *Duflon Industries*) that was incorporated in the year 1989. He claims that during the period 1989 to 2023 he had worked as a full-time employee of Duflon Industries and had also extended personal guarantees in respect of loans availed by the said company. The petitioner claims that Duflon Industries has since become a very successful enterprise and during the year 2023-24 recorded a turnover of ₹245 crores. The petitioner claims that the company employs 250 workers directly and almost equal number of workers indirectly. The petitioner is aggrieved inasmuch as he has been denied the benefit of participating in the gratuity fund on account of being a shareholder of Duflon Industries, who holds more than 5% of the issued equity capital.

3. The learned counsel for the petitioner referred to the decision of the Supreme Court in ***D.S.Nakara and Others v. Union of India, (1983) 1 SCC 305*** and submits that this is the apposite case for the court to take affirmative action and extend the benefit of admission to gratuity fund, to individuals who are otherwise not entitled by virtue of Rule 102 of the Income Tax Rules, 1961.

4. Rule 102 of the Income Tax Rules is set out below:

> "**Admission of directors to a fund.**
> 102. Where the employer is a company as defined in clause (i) of sub-section (1) of section 3 of the Companies Act, 1956 (1 of 1956), a director of the company may be admitted to the benefits of the fund only if he is a wholetime *bona fide* employee of the company and does not beneficially own shares in the company carrying more than five per cent of the total voting power."

5. We are unable to accept that the said rule violates Articles 14 and 21 of the Constitution of India as is contended by the petitioner. In terms of Section 36(1)(v) of the Act, any sum paid by an assessee as an employer by

way of contribution to an approved gratuity fund created by the employer for the exclusive benefit of the employees under an irrevocable trust, is allowable as a deduction for computing the income of the assessee. In terms of Section 10(10) of the Act, certain payments received as gratuity by an employee are excluded from the scope of income chargeable to tax. It is apparent that the rationale for not admitting directors who have substantial equity participation in the employer is to not grant exemption in respect of payments made by an employer company indirectly to its own shareholders. A person having substantial shares in a company but for the corporate veil would be considered as the same person.

6. Article 14 of the Constitution of India does not proscribe reasonable classification subject to the same having a reasonable nexus with the object of the legislation. In the present case, the object of granting exemption from certain income is to confer certain benefits to an employee and incentivise the companies to contributing to fund for the benefit of its employees. The tax concessions are coupled with safeguards to ensure that the contributions made by the employer to the gratuity fund are held in trust solely for the benefits of its employees. An employee who held substantial shares in a company clearly stands in a separate class when it comes to contributions towards gratuity.

7. We are unable to accept that the classification between employee directors of a company who do not own substantial beneficial shares in the company and those who do, for the purposes of payment of gratuity, is an unreasonable classification. It is also material to note that the directors of a company are effectively in control of the company. Thus, excluding a director who is not only in control of the company but has substantial equity

stake in the company from admission to an approved gratuity fund, cannot by any stretch be considered to be violative of the equal protection clause.

8. Insofar as violation of Article 21 is concerned, we are unable to accept that the denial of benefit of admission to a gratuity fund to a director employee who holds substantial equity interest in the fund would in any way deprive the director of right to life as understood in its expansive sense.

9. The petition is unmerited and accordingly dismissed.

ACTING CHIEF JUSTICE

TUSHAR RAO GEDELA, J

DECEMBER 09, 2024/tr

Click here to check corrigendum, if any