Reserved Judgment

IN THE HIGH COURT OF UTTARAKHAND AT NAINITAL

Writ Petition (M/S) No.577 of 2014

M/s J.B. Memorial Manas Academy Management Society
……. **Petitioner**

Versus

Chief Commissioner of Income Tax
…… **Respondent**

Mr. Mohit Maulekhi, Adv. for the petitioner.
Mr. H.M. Bhatia, Standing Counsel, for the respondent-Income Tax.

Reserved on: 09.11.2017
Delivered on: 17.11.2017

Hon'ble Rajiv Sharma , J.

Petitioner is a society, registered under the Societies Registration Act 1860, vide registration Certificate No.218/2004-2005 dated 15.07.2004. It was renewed vide renewal certificate dated 14.7.2009. The main purpose, aims and object, as stated in the Memorandum of Association of the Society, is to impart education along with ancillary objects. Petitioner has placed on record the copy of Memorandum of Association vide Annexure No.3. It is running educational institution in the name and style of 'J.B. Memorial Manas Academy, Pithoragarh'. Petitioner society applied for exemption u/s 10(23C)(iv) of the Income Tax Act, 1961 (*hereinafter to be referred as 'the Act')* on 05.9.2012. The case of the petitioner for exemption was rejected by the respondent vide the impugned order dated 20.9.2013, *inter alia*, on the ground that the Society had disproportionate fee structure which was devised to earn maximum money for the purpose of expansion of the institution. It is stated in the impugned order that the expansion of institution may not fall into the ambit of charitable activity.

2. Learned Counsel for the petitioner has argued that the respondent authority has erred in law in giving finding against the petitioner society. Petitioner society has to levy the fee as per law and the surplus amount, if any, is required to be invested for increasing the infrastructure and wherewithal. Construction of building is a *sine qua non* for imparting education. The school is also required to run buses to ferry the students. The school is also required to levy the computer fee. The primary purpose of the society is to impart education. Other ancillary objects are to be overlooked in view of the principal/main object. Learned counsel for the respondent has justified the impugned order.

3. The questions raised in this petition are no more *res integra* in view of the law laid down by their Lordships of Hon. Apex Court in 2008 (10) SCC 509 in the matter of '*American Hotel & Lodging Association Educational Institute v. CBDT*'. Their Lordships have held as under: -

"30. *In conclusion, learned counsel submits that there is no dispute that certain huge amount of Rs 1,30,30,288 has been remitted and that fact alone is conclusive circumstance to show that the appellant Institution is a commercial venture existing for profit and that it is not existing solely for educational purposes in India. The learned counsel urged that the third proviso brought in the concept of application of income vide the Finance Act, 1998 in order to bring about parity between universities and other educational institutions, on one hand, and public charitable trusts covered by Sections 11 and 12 under the 1961 Act. Therefore, according to the learned counsel, even at the stage of approval, the PA can take into account not only the nature, activities and genuineness of the Institute but also the manner in which the income derived in India is spent/utilised in India. The learned counsel submits that in view of the Finance Act, 1998, the provisions of Section 11(1)(a) have got to be read into the provisions of Section 10(23-C)(vi) and if so read the applicant Institute is required to state in its application as to how it has utilised its income in India in the year ending 31-3-1999. In this connection, learned counsel referred to Section 11(1)(a) which states that certain incomes shall not be included in the total income of the previous year of the person in receipt of such income if such income is derived from property held under trust, wholly for charitable or religious purposes, to the extent of which such income is applied to such purposes in India. The learned counsel submits that under Section 10(23-C)(vi) as well as the third proviso thereto, the words "in India" are not there but to give purposive interpretation to the said section the court should read those words into Section 10(23-C)(vi) to stop shifting of the "income"/profits accruing in India from being transferred to US. According to the learned counsel, when the appellant herein expatriated a*

sum of Rs 1,30,30,288 or Rs 1.14 crores (approx.) after taking into account expenses incurred by the HO to USA, it is clear that the appellant Institution has failed to comply with the requirements of Section 10(23-C)(vi) and, therefore, it is not entitled to approval. For the aforestated reasons, according to the learned counsel, no interference is called for in the present case.

33. *We also quote hereinbelow Section 11(1)(a) of the 1961 Act, which reads as follows:*

> *"11. Income from property held for charitable or religious purposes.—(1) Subject to the provisions of Sections 60 to 63, the following income shall not be included in the total income of the previous year of the person in receipt of the income—*
>
> > *(a) income derived from property held under trust wholly for charitable or religious purposes to the extent to which such income is applied to such purposes in India; and, where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of fifteen per cent of the income from such property;*

38. *In deciding the character of the recipient, it is not necessary to look at the profits of each year, but to consider the nature of the activities undertaken in India. If the Indian activity has no correlation with education, exemption has to be denied (see judgment of this Court in Oxford University Press[1]). Therefore, the character of the recipient of income must have character of educational institution in India to be ascertained from the nature of the activities. If after meeting expenditure, surplus remains incidentally from the activity carried on by the educational institution, it will not cease to be one existing solely for educational purposes. In other words, existence of surplus from the activity will not mean absence of educational purpose (see judgment of this Court in Aditanar Educational Institution v. CIT[4]). The test is—the nature of activity. If the activity like running a printing press takes place it is not educational. But whether the income/profit has been applied for non-educational purpose has to be decided only at the end of the financial year.*

39. *In Oxford University Press[1] this Court found that the applicant was a branch of Oxford Press which was part of Oxford University but its activity in India was restricted to publishing books, journals, periodicals, etc. The Tribunal held that because Oxford Press is part of the university its income was exempt under Section 10(22) as it stood at the relevant time. It is in this context that the words "existing solely for educational purposes and not for the purposes of profit" in Section 10(22), which words also find place in Section 10(23-C)(vi), came for consideration. This Court held that location of the university is not relevant, what is relevant is—whether there is imparting of education in India. Therefore, the test formulated by this Court to decide the character of the recipient of income under Section 10(22) is whether there is in fact existence of an activity which is in the nature of "imparting of education in India". This is how the words "in India" have come into judgment and not by incorporation from Section 11(1)(a) of the 1961 Act, as contended on behalf of the Department."*

4. Their Lordships of Hon. Supreme Court in 2015 (8) SCC 47 in the case of *Queen's Educational Society v. Commissioner of Income Tax* have held that the dominant object is to be applied whether the educational institution exists solely for educational purposes and not

for purposes of profit. Their Lordships have also explained the application of three requirements to seek exemption u/s 10(23-c)(vi) of the Income Tax Act as under: -

*"**5**. It will be noticed that Section 10(23-C)(iii-ad) has three requirements — (a) the educational institution must exist solely for educational purposes; (b) it should not be for purposes of profit; and (c) the aggregate annual receipts of such institution should not exceed the amount of annual receipts as may be prescribed. Such prescription is to be found in Rule 2-CA being an amount of Rs 1 crore.*

***6**. The said Section 10(23-C)(iii-ad) was inserted by Finance Act 2 of 1998 with effect from 1-4-1999. Prior thereto, the Income Tax Act had a corresponding section, namely, Section 10(22) which was as follows:*

"10. Incomes not included in total income.—In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—

** * **

(22) any income of a university or other educational institution, existing solely for educational purposes and not for purposes of profit;".

***11**. Thus, the law common to Sections 10(23-C)(iii-ad) and (vi) may be summed up as follows:*

(1) Where an educational institution carries on the activity of education primarily for educating persons, the fact that it makes a surplus does not lead to the conclusion that it ceases to exist solely for educational purposes and becomes an institution for the purpose of making profit.

(2) The predominant object test must be applied—the purpose of education should not be submerged by a profit-making motive.

(3) A distinction must be drawn between the making of a surplus and an institution being carried on "for profit". No inference arises that merely because imparting education results in making a profit, it becomes an activity for profit.

(4) If after meeting expenditure, a surplus arises incidentally from the activity carried on by the educational institution, it will not cease to be one existing solely for educational purposes.

(5) The ultimate test is whether on an overall view of the matter in the assessment year concerned the object is to make profit as opposed to educating persons.

***23**. The Punjab and Haryana High Court, by the impugned judgment dated 29-1-20102 expressed its dissatisfaction with the view taken by the Uttarakhand High Court in Queen's Educational Society1 as follows: (SCC OnLine P&H para 8.8)*

"8.8. We have not been able to persuade ourselves to accept the view expressed by the Division Bench of the Uttarakhand High Court in Queen's Educational Society1. There are variety of reasons to support our opinion. Firstly, the scope of the third proviso was not under consideration, inasmuch as, the case before the Uttarakhand High Court pertained to Section 10(23-C)(iii-ad) of the Act. The third proviso to Section 10(23-C)(vi) is not applicable to the cases falling within the purview of Section 10(23-C)(iii-ad). Secondly, the judgment rendered by the Uttarakhand High Court runs contrary to the provisions of Section 10(23-C)(vi) of the Act including the provisos thereunder. Section 10(23-C)(vi) of the Act is equivalent to the provisions of Section 10(22) existing earlier, which were introduced with effect from 1-4-1999 and it ignores the speech of the Finance Minister made before the introduction of the

said provisions, namely, Section 10(23-C) of the Act. (See observations in American Hotel & Lodging Assn. Educational Institute case9.) Thirdly, the Uttarakhand High Court has not appreciated correctly the ratio of the judgment rendered by the Hon'ble Supreme Court in Aditanar Educational Institution8 and while applying the said judgment including the judgment which had been rendered by the Hon'ble Supreme Court in Children Book Trust11, it lost sight of the amendment which had been carried out with effect from 1-4-1999 leading to the introduction of the provisions of Section 10(23-C) of the Act. Lastly, that view is not consistent with the law laid down by the Hon'ble Supreme Court in American Hotel & Lodging Assn. Educational Institute9."

It then summed up its conclusions as follows: (Pinegrove International Charitable Trust case2, SCC OnLine P&H para 8.13)

"8.13. From the aforesaid discussion, the following principles of law can be summed up:

(1) It is obligatory on the part of the Chief Commissioner of Income Tax or the Director, which are the prescribed authorities, to comply with proviso thirteen (un-numbered). Accordingly, it has to be ascertained whether the educational institution has been applying its profit wholly and exclusively to the object for which the institution is established. Merely because an institution has earned profit would not be the deciding factor to conclude that the educational institution exists for profit.

(2) The provisions of Section 10(23-C)(vi) of the Act are analogous to the erstwhile Section 10(22) of the Act, as has been laid down by the Hon'ble Supreme Court in American Hotel & Lodging Assn.9 To decide the entitlement of an institution for exemption under Section 10(23-C)(vi) of the Act, the test of predominant object of the activity has to be applied by posing the question whether it exists solely for education and not to earn profit (see five-Judge Constitution Bench judgment in Surat Art Silk Cloth Manufacturers' Assn.3). It has to be borne in mind that merely because profits have resulted from the activity of imparting education would not result in change of character of the institution that it exists solely for educational purpose. A workable solution has been provided by the Hon'ble Supreme Court in para 33 of its judgment in American Hotel & Lodging Assn. case9. Thus, on an application made by an institution, the prescribed authority can grant approval subject to such terms and conditions as it may deem fit provided that they are not in conflict with the provisions of the Act. The parameters of earning profit beyond 15% and its investment wholly for educational purposes may be expressly stipulated as per the statutory requirement. Thereafter the assessing authority may ensure compliance with those conditions. The cases where exemption has been granted earlier and the assessments are complete with the finding that there is no contravention of the statutory provisions, need not be reopened. However, after grant of approval if it comes to the notice of the prescribed authority that the conditions on which approval was given, have been violated or the circumstances mentioned in 13th proviso exists, then by following the procedure envisaged in 13th proviso, the prescribed authority can withdraw the approval.

(3) The capital expenditure wholly and exclusively to the objects of education is entitled to exemption and would not constitute part of the total income.

(4) The educational institutions, which are registered as a Society, would continue to retain their character as such and would be eligible to apply for exemption under Section 10(23-C)(vi) of the Act. (See para 8.7 of the judgment in Aditanar Educational Institution case8.)

(5) Where more than 15% of income of an educational institution is accumulated on or after 1-4-2002, the period of accumulation of

the amount exceeding 15% is not permissible beyond five years, provided the excess income has been applied or accumulated for application wholly and exclusively for the purpose of education.

(6) The judgment of Uttarakhand High Court rendered in Queen's Educational Society1 and the connected matters, is not applicable to cases which fall within the provisions of Section 10(23-C)(vi) of the Act. There are various reasons, which have been discussed in para 8.8 of the judgment, and the judgment of the Allahabad High Court rendered in City Montessori School13 lays down the correct law."

And finally held: (SCC OnLine P&H paras 8.15 & 8.16)

"8.15. As a sequel to the aforesaid discussion, these petitions are allowed and the impugned orders passed by the Chief Commissioner of Income Tax withdrawing the exemption granted under Section 10(23-C)(iv) of the Act are hereby quashed. However, the Revenue is at liberty to pass any fresh orders, if such a necessity is felt after taking into consideration the various propositions of law culled out by us in para 8.13 and various other paras.

8.16. The writ petitions stand disposed of in the above terms."

***24**. The view of the Punjab and Haryana High Court has been followed by the Delhi High Court in St. Lawrence Educational Society v. CIT14. Also in Tolani Education Society v. Director of Income Tax (Exemption)15, the Bombay High Court has expressed a view in line with the Punjab and Haryana High Court's view, following the judgments of this Court in Surat Art Silk Cloth Manufacturers' Assn. case3 and Aditanar Educational Institution case8 as follows: (Tolani Education Society case15, SCC OnLine Bom para 13)*

"13. … The fact that the petitioner has a surplus of income over expenditure for the three years in question, cannot by any stretch of logical reasoning lead to the conclusion that the petitioner does not exist solely for educational purposes or, as that Chief Commissioner held that the petitioner exists for profit. The test to be applied is as to whether the predominant nature of the activity is educational. In the present case, the sole and dominant nature of the activity is education and the petitioner exists solely for the purposes of imparting education. An incidental surplus which is generated, and which has resulted in additions to the fixed assets is utilised as the balance sheet would indicate towards upgrading the facilities of the college including for the purchase of library books and the improvement of infrastructure. With the advancement of technology, no college or institution can afford to remain stagnant. The Income Tax Act, 1961 does not condition the grant of an exemption under Section 10(23-C) on the requirement that a college must maintain the status quo, as it were, in regard to its knowledge-based infrastructure. Nor for that matter is an educational institution prohibited from upgrading its infrastructure on educational facilities save on the pain of losing the benefit of the exemption under Section 10(23-C). Imposing such a condition which is not contained in the statute would lead to a perversion of the basic purpose for which such exemptions have been granted to educational institutions. Knowledge in contemporary times is technology driven. Educational institutions have to modernise, upgrade and respond to the changing ethos of education. Education has to be responsive to a rapidly evolving society. The provisions of Section 10(23-C) cannot be interpreted regressively to deny exemptions. So long as the institution exists solely for educational purposes and not for profit, the test is met."

5. The Division Bench of Bombay High Court in 2010 (327) ITR 121 in the matter of '*Vanita Vishram Trust*

v. Chief Commissioner of I.T.' has held that the Trust is vested with primary object to provide education. Other objects mentioned in Trust are not relevant. Their Lordships have held as under: -

"*12. In so far the aspect of surplus is concerned, one must in addition, advert to the provision which has been made by Parliament in the third proviso to Section 10(23C). By the third proviso, it has been clarified that in the case inter alia of Universities or other educational institutions which have applied its income or accumulated it for application wholly and exclusively to the objects for which it is established and in a case where fifteen per cent of income is accumulated on or after 1 April 2002, the period of the accumulation of the amount exceeding fifteen per cent, shall in no case exceed five years. This provision would establish that Parliament did not regard the accumulation of income by a University or educational institution governed by subclause (vi) as a disabling factor, so long as the purpose of accumulation is the application of the income wholly and exclusively to the objects for which the institution has been established. Parliament has, however, prescribed that where more than fifteen per cent of the income is accumulated after 1 April 2002, the amount exceeding fifteen per cent shall not be accumulated for a period in excess of five years.*

13. For all these reasons, we are of the view that the rejection of the approval by the First Respondent was manifestly misconceived. Only two reasons have weighed with the First Respondent in rejecting the approval, both of which have been found to suffer from manifest error. In Aditanar Educational Institution (supra), the Supreme Court, while construing the provisions of Section 10(22), held that the availability of exemption should be evaluated each year to find out whether the institution has existed during the relevant year solely for educational purposes and not for the purposes of profit. If after meeting the expenditure, a surplus results incidentally from an activity lawfully carried on by the educational institution, the institution will not cease to be one existing solely for educational purposes since the object is not to make profit. The decisive or acid test, the Supreme Court observed, is whether on an overall view of the matter, the object is to make a profit. In evaluating or appraising the issue, the Supreme Court noted that one should bear in mind the distinction between the corpus, the objects and the powers of the concerned entity.

14. The First Respondent while rejecting the applications of the Petitioner has adverted to the judgment of the Uttarakhand High Court in Commissioner of Income Tax v. Queens' Educational Society MANU/UC/0174/2007 : (2009) 319 ITR 160 The statement of facts as recited in the judgment of the High Court is to the effect that the assessee had a profit of thirty per cent in Assessment Year 200001 and twenty seven per cent in Assessment Year 200102. The assessee was conducting an educational institution. The Tribunal held that the assessee was entitled to the benefit of the exemption under Section 10(23C). The High Court observed that 'the law is well settled that if the profit is proved by an educational society then that will be the income to the Society as the surplus amount remains in the account books of the society after meeting all the expenses incurred towards imparting the education'. A reference was made to the judgment of the Supreme Court in Aditanar (supra). The judgment of the Supreme Court was, however, distinguished on the ground that the objects clause of the assessee indicated that while there were other objects to be achieved, the assessee had done nothing except to pursue the main

object of providing education and earning profit. Moreover, with the profit earned, the assessee had strengthened its capacity to earn more, rather than to undertake any other activities to fulfill the other objects for which the trust was constituted. Though the Trust had made an investment in fixed assets like furniture and buildings which may be connected with the imparting of education this, the High Court held, was with a view to expanding the institution and to earn more income.

15. If the facts as they appear in the judgment of the Uttarakhand High Court are considered, the case would be entirely distinguishable. The judgment of the High Court would indicate that the assessee in that case was construed to be one which existed with the object of enhancing the income and of earning profits as opposed to the provision of education. However, it would be necessary for this Court to observe that some of the observations contained in the judgment of the Uttarakhand High Court may not be in conformity with the law laid down by the Supreme Court in Aditanar's case (supra). The High Court took exception to the conduct of the assessee on the ground that though it was entitled to pursue other 'noble and pious' objects, the assessee had done nothing to achieve them and had only pursued the main object of providing education and earning profit. Now, it must be appreciated that in order to obtain the benefit of the exemption under Section 10(23C)(vi), the University or, as the case may be, educational institution must exist solely for educational purposes and not for the purposes of profit. The requirement that the institution must exist solely for educational purposes would militate against an institution pursuing other objects. Consequently, the High Court was, in our view and with due respect, not correct in holding as a principle of law that the benefit of the exemption should be denied on the ground that the assessee has only pursued its main object of providing education and had not pursued the other objects for which the Trust was constituted. Were the assessee to pursue other objects, it would clearly run afoul of subclause (vi). The assessee must exist solely for educational purposes. In this view of the matter, while we hold that the facts of the present case are distinguishable, we have also recorded our reservations about the correctness of the statement of legal principle in the judgment of the Uttarakhand High Court. The attention of the Court has also been drawn to the fact that a Division Bench of the Punjab and Haryana High Court in Pinegrove International Charitable Trust v. Union of India CWP 6031 of 2009 decided on 29 January 2010 has also expressed reservation about the view of the Uttarakhand High Court in Queens' Educational Society (supra)."

6. The Division Bench of Allahabad High Court in (2013) 36 Taxmann.com 105 (Allahabad) in the matter of '*Neeraj Janhitkari Gramin Sewa Sansthan v. CCIT*' has held that the application was maintainable to seek exemption on behalf of the society. Their Lordships have held as under: -

"12. The next question which now arises for consideration is whether an application can be rejected on the ground that the memorandum of association of the society provides for various other objects apart from educational activities. In this regard, the argument of learned counsel for the petitioner is that even though under the unamended bye-laws of the society, various other aims and objects were mentioned but according to application for approval and the material on record, the society is only carrying on educational activities. In this regard,

specific assertion has been made in para 2 of the application for approval. In para 7 of the application, there is a specific assertion that the only source of income of the society is the nominal fees being charged from students and it has no other source of income. Learned counsel for the petitioner has placed strong reliance on the judgment of this Court in the case of C.P. Vidya Niketan Inter College Shikshan Society (supra). We find that there the petitioner was a society which had made an application for approval under s. 10(23C)(vi) and its application for approval was rejected on the ground that benefit of s. 10(23C)(vi) is available only to an educational institution existing solely for the purpose of imparting education, while the application has been made by a society having many activities that appear to be other than educational such as to make appropriate efforts for upliftment of public in social and cultural field etc. Therein, this Court had held that even though the aims and objects of the society may contain several objects but if it has been proved by material on record that the society is not perusing any other activity apart from education then in such case, the society will qualify for grant of approval under s. 10(23C)(vi) of the Act. It was observed as under:

In the facts and circumstances, we are of the opinion that as of now the petitioner society running educational institution by the name of C.P. Vidya Niketan Inter College at Kaimganj, District Farrukhabad imparts education to students from Class VI to XII, in the absence of any allegation or material, the object clause providing for other charitable activities, would not disentitle the society from approval under s. 10(23C)(vi) of exemption. The proviso added to s. 10(23C)(vi), specially provisos 2, 3, 12 and 13, give sufficient powers to check the abuse of the exemption. The mere possibility, therefore, that the society may in future pursue activities, which are not charitable, or closely connected with education for making profit, would not constitute the grounds to reject the approval under s. 10(23C)(vi).

13. Perusal of the impugned order shows that the pleading in this regard has not been taken into consideration. Further, in the impugned orders, although, there is a finding that the society is having many objects other than educational, but there is no application of mind to the assertion made by the society that it is only pursuing the educational activity and no other. In view of the Division Bench decision of this Court in case of C.P. Vidya Niketan Inter College Shikshan Society (supra), in case, the society is pursuing only educational objects and no other activity then the application by such a society for grant of approval under s. 10(23C)(vi) cannot be rejected on the ground that its aims and objects contain several other objects apart from educational and application by such a society is perfectly maintainable."

7. Accordingly, the writ petition is allowed. Impugned order dated 20.09.2013 (Annexure No.1) passed by the respondent is quashed and set aside. The respondent-Chief Commissioner of Income Tax is directed to grant exemption to the petitioner-Society for the relevant assessment year. No order as to costs.

(Rajiv Sharma, J.)

Rdang