

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

TAX APPEAL NO. 608 of 2016

With

TAX APPEAL NO. 609 of 2016

With

TAX APPEAL NO. 741 of 2016

TO

TAX APPEAL NO. 744 of 2016

For Approval and Signature:

HONOURABLE MR.JUSTICE M.R. SHAH

Sd/-

and

HONOURABLE MR.JUSTICE B.N. KARIA

Sd/-

1	Whether Reporters of Local Papers may be allowed to see the judgment ?	Yes
2	To be referred to the Reporter or not ?	Yes
3	Whether their Lordships wish to see the fair copy of the judgment ?	No
4	Whether this case involves a substantial question of law as to the interpretation of the Constitution of India or any order made thereunder ?	No

PRINCIPAL COMMISSIONER OF INCOME TAX-2....Appellant(s)

Versus

GULMOHAR GREEN GOLF AND COUNTRY CLUB LTD....Opponent(s)

Appearance:

MR MANISH BHATT, SR. ADVOCATE with MRS MAUNA M BHATT, ADVOCATE for the Appellant(s) No. 1

MR SN SOPARKAR, SR. ADVOCATE with MR BS SOPARKAR, CAVEATOR for the Opponent

CORAM: HONOURABLE MR.JUSTICE M.R. SHAH

and

HONOURABLE MR.JUSTICE B.N. KARIA

Date : 16/11/2016

COMMON ORAL JUDGMENT

(PER : HONOURABLE MR.JUSTICE M.R. SHAH)

[1.0] As common question of law and facts arise in this group of

appeals, they are disposed of by this common judgment and order.

Tax Appeal No.608/2016

[2.0] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Income Tax Appellate Tribunal, Ahmedabad in ITA No.2337/Ahd/2011 for the AY 2008-09 by which the learned Tribunal has dismissed the said appeal preferred by the Revenue, the Revenue has preferred the present Tax Appeal raising the following substantial question of law.

“Whether, the Income Tax Appellate Tribunal has substantially erred in law and on facts, in deleting the addition, of Rs.1,75,15,680/- made on account of receipt of membership fees treating the same as Capital Receipt?”

Tax Appeal No.609/2016

[2.1] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Income Tax Appellate Tribunal, Ahmedabad in ITA No.2054/Ahd/2011 for the AY 2008-09 by which the learned Tribunal has dismissed the said appeal preferred by the Revenue, the Revenue has preferred the present Tax Appeal raising the following substantial question of law.

“Whether, the Income Tax Appellate Tribunal has substantially erred in law and on facts, in deleting the addition, of Rs.1,75,15,680/- made on account of receipt of membership fees treating the same as Capital Receipt?”

Tax Appeal No.741/2016

[2.2] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Income Tax Appellate Tribunal, Ahmedabad in ITA No.3301/Ahd/2015 for the AY 2011-12 by which the learned Tribunal has dismissed the said appeal preferred by the

Revenue, the Revenue has preferred the present Tax Appeal raising the following substantial question of law.

“Whether, the Income Tax Appellate Tribunal has substantially erred in law and on facts, in deleting the addition, of Rs.2,29,50,600/- made on account of receipt of membership fees treating the same as Capital Receipt?”

Tax Appeal No.742/2016

[2.3] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Income Tax Appellate Tribunal, Ahmedabad in ITA No.54/Ahd/2016 for the AY 2011-12 by which the learned Tribunal has dismissed the said appeal preferred by the Revenue, the Revenue has preferred the present Tax Appeal raising the following substantial question of law.

“Whether, the Income Tax Appellate Tribunal has substantially erred in law and on facts, in deleting the addition, of Rs.2,29,50,600/- made on account of receipt of membership fees treating the same as Capital Receipt?”

Tax Appeal No.743/2016

[2.4] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Income Tax Appellate Tribunal, Ahmedabad in ITA No.3302/Ahd/2015 for the AY 2012-13 by which the learned Tribunal has dismissed the said appeal preferred by the Revenue, the Revenue has preferred the present Tax Appeal raising the following substantial question of law.

“Whether, the Income Tax Appellate Tribunal has substantially erred in law and on facts, in deleting the addition, of Rs.1,95,78,000/- made on account of receipt of membership fees treating the same as Capital Receipt?”

Tax Appeal No.744/2016

[2.5] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Income Tax Appellate Tribunal, Ahmedabad in ITA No.3671/Ahd/2015 for the AY 2012-13 by which the learned Tribunal has dismissed the said appeal preferred by the Revenue, the Revenue has preferred the present Tax Appeal raising the following substantial question of law.

“Whether, the Income Tax Appellate Tribunal has substantially erred in law and on facts, in deleting the addition, of Rs.1,95,78,000/- made on account of receipt of membership fees treating the same as Capital Receipt?”

[3.0] For the sake of convenience, Tax Appeal No.608/2016 is treated as a lead matter. At the outset it is required to be noted that the dispute is with respect to common assessee, however with respect to different years and there are common question of facts and law in this group of Tax Appeals.

[4.0] That the assessee is carrying on the business of club activities in the name and style of Gulmohar Green Gold and Country Club Ltd. That the assessee filed return of income on 29.09.2008 for AY 2008-09 declaring total income of Rs.1630/-. That the said return of income was processed under Section 143(1) of the Income Tax Act, 1995 (hereinafter referred to as “Act”). The case was selected for scrutiny and the notice under Section 143(2) of the Act was duly issued and served upon the assessee. On verification of the return of income and other details furnished, the Assessing Officer noticed the business of club activities carried out by the assessee and also the main object of the assessee company. On further scrutiny of the accounts it was noticed by the Assessing Officer that the assessee has enrolled members on payment of security deposit as entrance fee. It was noticed by the AO that the said

security deposit though was refundable to the members after 25 years, however without interest. It was noticed by the AO that company had only a mere share capital of Rs.5,10,000/- only and whatever amount collected as security deposits from the members as entrance fees was utilized for construction and providing other facilities at the club. The AO noticed that the assessee has not kept apart the security deposit obtained from the members but appropriated the same for construction and other amenities provided in the club. The AO also noticed that the deposits collected from the members has not been shown under the head “liabilities” in the accounts of the assessee. Therefore, a detailed show-cause notice dated 12.11.2010 was duly issued and served upon the assessee asking to show cause as to why the security deposits collected from the members should not be treated as membership fees and the same may not be treated as current years’ receipts / income of the year under consideration. The show-cause notice reads as under:

“2. During the course of assessment proceedings, it is noticed that during the year under assessment you have obtained security deposit of Rs.3,12,78,000/- from the members which has been shown in the balance-sheet under the head “unsecured loans”. The total such deposits collected by the assessee from the members till date comes to Rs.14,54,01,000/-. From the discussion the undersigned had with you, it is transpired that for joining as member of the Club you have not charged any membership fees but taken security deposit which is refundable after 25 years without interest. On an analysis of the Balance-sheet, it will be seen that the share capital available with the company is only Rs.5,10,000/- only. However, the Club has constructed immovable properties and prepared the golf turf to the extent of Rs.9 crores and made investments of Rs.4.20 Crores. From the above it is clear that the assessee has not kept apart the security deposits obtained from the Members but appropriated the deposits obtained from the members for the construction activities of the club and investment purposes. It is further noticed that you have not shown the deposits received from the Members under the head “Liabilities” in your accounts and as such it was clearly an income receipt arising in the course of your normal business activities.

3. As per the Articles of Association of the Company, the enrollment of members are governed by Articles 2(a) and (b) of the

Articles of Association of the Company. For ready reference the same are re-produced hereunder:

2.(a) The Board of Directors of the company may enroll various categories of Club members on payment of such Non-interest bearing refundable security deposit as may be decided from time to time, to avail the club facilities provided by the Club. The Club members will have no rights as member of the company unless they hold share(s) in the Company. The Club members shall not have the management rights and accordingly, would not be entitled to receive notices of general meetings and attending or voting at the general meetings.

(b) (i) the Non-interest bearing refundable Security Deposit by way of entrance fee and Annual Subscription fee shall be collected from different classes of club members as may be decided by the Board of Directors of the company or a committee appointed by the Board of Directors for the purpose.

(ii) The Non-interest bearing refundable Security Deposit shall be refunded as per the law, to the member, or to his legal heir or nominee after 25 years from the date of enrollment as Club Member.

On a plain reading the above Articles, it will be seen that the members who are interested to join as members of the Club are required to pay Security Deposit as entrance fees and the members are also required to pay Annual Subscription fee and other charges for the amenities availed by the members as collected from different classes of club members as may be decided by the Company from time to time. Hence, it is clear that only payment of Security Deposit one can enroll as member of the Club for availing the facilities offered by the Club.

4. It is further noticed that the assessee is following mercantile system of accounting. Section 5(1) defines the scope of total income in case of a resident and includes all income which -

- (a) Is received or is deemed to be received in India in such year by or on behalf of such person; or*
- (b) Accrues or arises or is deemed to accrue or arise to him in India during such year; or*
- (c) Accrues or arises to him outside India during such year.*

It is well settled that two conditions are necessary to say that income has accrued to or earned by the assessee. They are (i) it is necessary that the assessee must have contributed to its accruing or arising by rendering services or otherwise, and (ii) a debt must have come into existence and he must have acquired a right to receive the payment. In the instant case, a debt was created in favour of the

assessee immediately on enrollment of a person as member. Once the member is enrolled, the assessee Club was bound to provide facilities to the members. In the present case, considering the observation made above, the assessee has fulfilled the first two conditions and as such the security deposit obtained by the Club/assessee from the members as entrance fees is nothing but membership fees which required to be treated as revenue receipt. Further, the money collected in the form of security deposit by the assessee Club becomes its exclusive asset. Over and above the members are liable to pay Annual Subscription fees and other charges for the amenities availed at the Club on actual basis. In essence, a person becoming member after paying the security deposit as entrance fees has a right to avail all the facilities available at the Club and also have a right to transfer the membership to any person. Therefore, I am of the view that you have obtained membership fees from the members in the guise security deposits instead of membership fees so as to defeat the provisions of Income-tax Act, 1961. I, therefore, propose to treat the security deposit collected by you from the members as membership fees and to finalise the assessment accordingly.

5. The issue of the deposit being 'refundable' has also been examined by this office. There is no dispute that the deposit is interest free and refundable after 25 years. The funds so received have been utilized for creating the facilities in which, as discussed above, the deposit payer has no interest or share. Hence, if at all, the depositor is eligible to claim refund of "current value" of the deposit after 25 years that is to say if he has advanced an amount of Rs.100/- now, and he will receive this amount i.e. 'Rs.100/-' after 25 years, at current prevailing interest rate of 12%, the current value of Rs.100/- paid to him after 25 years will be only Rs.5/-. Therefore, while he has paid a deposit of Rs.100/- at present value, he will be refunded only Rs.5/- at present value. Hence, in respect of all your deposits received during the year, it is proposed to treat the deposits accepted during the year as current year receipts after reducing the current value of "refundable component".

6. It is further noticed from the Memorandum of Association and Articles of Association of the Company that accepting of deposits from the Public is not an object of the company. In your case you have accepted the deposits from public prior to enrollment as members and as per the provisions of Companies Act, 1956 only those companies who have fulfilled the terms and conditions of Section 58A and 58AA can accept the deposits from the public. In view of this also, the security deposits collected by you is to be treated as current year's receipt.

7. It is noticed from the statement of total income that you have earned dividend income of Rs.41,70,484/- which is exempt. In this

regard, you are requested to show cause as to why the expenses incurred for earning such exempted income should not be disallowed u/s. 141 of the Act, r.w. Rule 8D of the Income Tax Rules, 1962.

8. Your reply, if any, should reach the undersigned on or before 29.11.2010 positively. If no reply is received within the stipulated time, it will be presumed that you have nothing to say in the matter and the assessment will be finalized as proposed above, which please note.”

[4.1] In response to the show-cause notice the assessee approached the Additional Commissioner of Income Tax, Range-IV, Ahmedabad vide application under Section 144A of the Act. Therefore, the matter was referred to the Additional CIT by the assessee under Section 144A of the Act for issuance of directions for framing the assessment. Accordingly, the Additional Commissioner of Income Tax, Range-IV, Ahmedabad issued directions vide his letter dated 22.12.2010. That after considering the directions issued by the Additional Commissioner of Income Tax, Range-IV, Ahmedabad vide letter dated 22.12.2010, the AO held that 60% of the security deposit received by the assessee during the year under assessment be considered as income for the year under assessment. The learned AO observed that the total security deposits collected by the assessee during the year comes to Rs.3,12,78,000/-; 60% of which comes to Rs.1,87,66,800/-. Therefore, the AO made an addition of Rs.1,87,66,800/- to the return income of the assessee for the year under consideration.

[4.2] Feeling aggrieved and dissatisfied with the addition of Rs.1,87,66,800/- made on account of receipt of membership fees treating the same as income for the year under assessment, the assessee preferred an appeal before the learned CIT(A). It was submitted before the learned CIT(A) that the learned AO has materially erred in making addition of Rs.1,87,66,800/- treating it as income for the year of assessment. In the alternative it was submitted that the security deposit

may be spread over a period for taxation i.e. to spread it over the life of membership. That the learned CIT(A) confirmed the addition of Rs.1,87,66,800/- treating it as an income, however the learned CIT(A) opined that the non-interest bearing security deposits refundable after 25 years received by the assessee from its all category members is not assessable as income only for the year under consideration and as the security deposits are considered as membership for the entire 25 years, the membership will be taxable equally for the entire period of 25 years and therefore, the learned CIT(A) considered 1/25th of the security deposit as income in the year of assessment and therefore, addition was restricted to Rs.12,51,120/- only.

[4.3] Feeling aggrieved and dissatisfied with the order passed by the learned CIT(A), both the Revenue as well as the assessee preferred respective appeals before the learned Income Tax Appeal Tribunal, Ahmedabad (hereinafter referred to as “Tribunal”). The learned Tribunal relying upon the decision of the Hon’ble Supreme Court in the case of **S.S. Sakhar Karkhana Ltd. vs. CIT, Kolhapur** reported in (2004) 270 ITR 1 (SC) and the decision of the Division Bench of this Court in the case of **Unique Mercantile Services Pvt. Ltd. in Tax Appeal No.1471 to 1478 of 2005** has allowed the appeal preferred by the assessee and has dismissed the appeal preferred by the Revenue and has ordered deletion of Rs.1,75,15,680/- made by the AO on account of receipt of membership fees by treating the same as Capital Receipt.

[4.4] Feeling aggrieved and dissatisfied with the impugned judgment and order passed by the learned Tribunal, the Revenue has preferred the Tax Appeal Nos.608/2016 and 609/2016. With respect to the subsequent assessment years the learned Tribunal has held in favour of the assessee and therefore, the Revenue is before this Court by way of Tax Appeal Nos.741/2016 to 744/2016 to consider the above substantial

question of law.

[5.0] Shri Manish R. Bhatt, learned Counsel has appeared on behalf of the Revenue and Shri S.N. Soparkar, learned Counsel has appeared on behalf of the assessee, who has appeared on caveat.

[6.0] Shri Bhatt, learned Counsel appearing on behalf of the Revenue has vehemently submitted that in the facts and circumstances of the case the learned Tribunal has materially erred in directing to delete the addition of Rs.1,75,15,680/- made by the AO on account of receipt of membership fees.

[6.1] It is submitted that the learned Tribunal has materially erred in relying upon the decision of the Hon'ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra). It is vehemently submitted by Shri Bhatt, learned Counsel appearing on behalf of the Revenue that in the present case the security deposit is though refundable after 25 years, the same shall be refunded without any interest. Therefore, the said security deposit will be interest free and considering the fact that the assessee had utilized the said security deposits from the members, for construction and providing other facilities at the club, the learned Tribunal ought not to have treated it as a Capital Receipt and ought to have treated it as an income as held by the learned AO.

[6.2] It is further submitted by Shri Bhatt, learned Counsel appearing on behalf of the Revenue that even the assessee has not kept apart the security deposit receipt from the members but appropriated the same for construction and other amenities provided in the club. It is submitted that as such the assessee company was having only a mere share capital of Rs.5,10,000/- and whatever amount collected as security deposits from the members, as stated hereinabove, has been utilized for

construction and providing other facilities at the club. It is submitted that therefore in the facts and circumstances of the case, the learned Tribunal has materially erred in relying upon and following the decision of the Hon'ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra).

While making above submissions, Shri Bhatt, learned Counsel appearing on behalf of the Revenue has heavily relied upon the decision of the Hon'ble Supreme Court in the case of **Income Tax Commissioner, Lucknow vs. Bazpur Co-op. Sugar Factory Ltd.** reported in 1988 (172) ITR 321 and the decision of the Division Bench of this Court in the case of Unique Mercantile Services Pvt. Ltd. (Supra).

[7.0] All these Tax Appeals are vehemently opposed by Shri S.N. Soparkar, learned Counsel appearing on behalf of the Assessee. Relying upon the decision of the Hon'ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra) in which the Hon'ble Supreme Court did consider the earlier decision in the case of Bazpur Co-op. Sugar Factory Ltd. (Supra) and after considering the said decision the Hon'ble Supreme Court set aside the order passed by the High Court, it is submitted that even in the case before the Hon'ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra), the deposit which was recovered by the society, was utilized and used for repayment of the loan of the society. It is submitted that therefore considering the direct decision of the Hon'ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra), the learned Tribunal has rightly deleted the addition made by the AO of Rs.1,75,15,680/- treating the same as Capital Receipt.

[7.1] Now, so far as the reliance placed upon the decision of the Division Bench of this Court in the case of Unique Mercantile Services Pvt. Ltd. (Supra) relied upon by the learned Counsel for the Revenue is concerned, it is vehemently submitted by Shri Soparkar, learned Counsel

appearing on behalf of the assessee that the said decision shall not be applicable to the facts of the case on hand. It is submitted that in the case before the Division Bench, it was a question of “fees” spread over and collected during the span of 15 years and infact the same was non-refundable and the issue before the Division Bench was that “fees” received during such years can be considered in the first year in which it was received and/or the same was required to be spread over upto 15 years. It is submitted that therefore in the facts and circumstances of the case, decision of the Division Bench in the case of Unique Mercantile Services Pvt. Ltd. (Supra) shall not be applicable to the facts of the case on hand more particularly when there was no question before the Division Bench as to whether such refundable security deposit shall be treated as an income or not.

[7.2] It is further submitted by Shri Soparkar, learned Counsel appearing on behalf of the assessee that in the present case not only the security deposit is refundable after 25 years, the interest earned by the club on such deposit is subjected to tax as income and the club is also paying tax on interest earned on such deposit. It is submitted that even after collecting the security deposit, as and when the member uses any activity offered at the club, necessary payments for such usage is always paid by the member.

Making above submissions and relying upon the decision of the Hon’ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra), it is requested to dismiss the present Tax Appeals and answer the question in favour of the assessee and against the Revenue.

[8.0] Heard the learned Counsel appearing for respective parties at length.

[8.1] The short but interesting question of law which arise for

determination of this Court is whether the receipt of membership fees, which is refundable after a period of 25 years but without interest, is required to be treated as income / revenue in the hands of the assessee or the same is to be treated as Capital Receipt?

[8.2] While considering the aforesaid question Article of Association of the assessee and the relevant Rules, Regulations and Bye-laws of the assessee with respect to the club members and security deposit are required to be referred to which are as under:-

Article of Association

2.(a) *The Board of Directors of the company may enroll various categories of Club members on payment of such Non-interest bearing refundable security deposit as may be decided from time to time, to avail the club facilities provided by the Club. The Club members will have no rights as member of the company unless they hold share(s) in the Company. The Club members shall not have the management rights and accordingly, would not be entitled to receive notices of general meetings and attending or voting at the general meetings.*

(b) (i) *the Non-interest bearing refundable Security Deposit by way of entrance fee and Annual Subscription fee shall be collected from different classes of club members as may be decided by the Board of Directors of the company or a committee appointed by the Board of Directors for the purpose.*

(ii) *The Non-interest bearing refundable Security Deposit shall be refunded as per the law, to the member, or to his legal heir or nominee after 25 years from the date of enrollment as Club Member.*

Rules, Regulations and Bye-Laws

“1. Club Members

The Club may enroll members on payment of security deposit to avail the facilities provided by the club. The Club members will have no rights as member of the Company unless they hold some shares in the Company. The Club members shall not have the management rights and accordingly would not be entitled to receive notices of general meetings, attending or voting at general meetings, nor be entitled to contest the election for

directorship of the Company.

2. Security Deposit:

- (1) *A Refundable Non-interest bearing Security Deposit shall be collected from different classes of club members as may be decided by the Board of Directors of the Company from time to time.*
 - (2) *No interest will be paid on security deposit collected from club members as mentioned in sub clause (1) above.*
 - (3) *Security deposit shall be refunded if a club member is dissolved or wind up as the case may be. In other cases, the security deposit shall be refunded to the member on expiry of 25 years and this period may be extended by a maximum period of 15 years (for 5, 10 or 15 years) at the discretion of the Club member to avail club facilities for the extended period. The security Deposit would not be refunded if the club membership is extended and only after the said period is over, the security deposit would be refunded.*
 - (4) *It is expressly provided that the Company shall not change above sub-clauses (1) to (4) above.*
5. *No Club member would be entitled by way of a right to claim refund of his security deposit before 25 years. However, the Club will have a right to refund the security deposit before expiry of this period and such person would not be entitled to avail the club facilities thereafter.*
6. *In case the Security Deposit is refunded earlier than the period of 25 years, the person shall cease to be a club member automatically.”*

[8.3] Considering the Articles of Association and the relevant Rules, Regulations and Bye-Laws of the assessee, the security deposit collected by the assessee at the time of enrollment of the club members is refundable after a period of 25 years and/or on happening of the eventuality in Rule / Bye Law No.2 i.e. if a club member dies or institutional member is dissolved or wind up as the case may be. In other cases the security deposit shall be refunded to the member on expiry of 25 years and the said period may be extended by maximum period of 15 years at the discretion of the club member to avail club facilities for the

extended period. It is also true that the said security deposit shall be non-interest bearing refundable security deposit. In light of the above the question posed for consideration of this Court is required to be considered i.e. whether such refundable security deposit shall be considered as revenue / income as sought to be contended on behalf of the revenue or Capital Receipt as contended on behalf of the assessee.

[8.4] It is the case on behalf of the Revenue that as security deposit is non-refundable interest deposit and that the same is utilized / used by the assessee for construction and providing other facilities at the club and that the said security deposit has not been kept apart the same cannot be treated as Capital Receipt, but the same is required to be considered as revenue / income in the hands of the assessee. In support of their above submissions, the Revenue has heavily relied upon the decision of the Hon'ble Supreme Court in the case of Bazpur Co-op. Sugar Factory Ltd. (Supra).

On the other hand it is the case on behalf of the assessee that merely because the security deposit is non-refundable interest security deposit and merely because the same is not kept apart and merely because the same is used by the assessee for some other purpose, the same does not denude the amount of its character of "deposit" carrying with it the obligation to repay. In support of their above submissions learned Counsel appearing on behalf of the assessee has heavily relied upon the decision of the Hon'ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra).

[8.5] In the case of S.S. Sakhar Karkhana Ltd. (Supra), the Hon'ble Supreme Court had an occasion to consider its earlier decision in the case of Bazpur Co-op Sugar Factory Ltd. (Supra). After considering the decision of the Hon'ble Supreme Court in the case of Bazpur Co-op

Sugar Factory Ltd. (Supra), the Hon'ble Supreme Court has observed in paras 21, 22, 24, 28, 30, 31, 32 as under:

"21. The Court reiterated the principle that "it is the true nature and quality of the receipt and not the head under which it is entered in the account books as would prove decisive" and that it makes no difference that the disputed amounts have been referred to as deposits and proceeded to consider the crucial issue in that light.

22. How far the ratio of the decision in Bazpur case could be applied to the case on hand is the first and foremost controversy. In the present case, the purchase and payment of price of sugarcane is undoubtedly part of trading operations of the assessee. It is in the course of such trading operations that the assessee realized the amounts (treated as deposits) with regularity and utilized the money so received in its business. To the extent the full payment is not made to the farmers, the assessee saved the raw material cost as well.

24. However, it needs to be clarified that the line of inquiry, in order to determine the true nature and character of the receipts, does not stop at ascertaining the mere fact whether the realization was in the course of trading operations. The moment it is found that certain amounts were deducted by the assessee out of the price payable to its members who supplied the raw material, the conclusion does not necessarily follow that all such realizations get impressed with the character of revenue receipts, giving rise to taxable income in the hands of the assessee. It is not any and every receipt linked to the trading activity that acquires the quality of revenue receipt. The Tribunal or the Court should go further and delve into the true nature, character and purpose of the realizations. If the amounts are meant to be held as deposits liable to be returned to the depositor at a specified point of time or on the happening of specified contingencies which are by no means uncertain or is otherwise treated as members' money - the depository having no unfettered dominion over the said funds, then, it is difficult to characterize them as the income of the assessee. The realization of monies from the grower-members in the course of trading operations could as well be construed to be an occasion, mode or convenient point of time at which the 'deposit' could be collected. Perhaps keeping this legal position in view, notwithstanding what has been stated in the earlier portion of the judgment, the learned Judges proceeded to address the next question, i.e. whether the receipts by way of deductions could be regarded as deposits as described in the bye-laws. While answering that question in the negative, the Court pointed out that it is the true nature and quality of the receipt that is material but not the head under which it is entered in the account books - a principle which is reiterated in a catena of decisions. The Court then

went on to conclude that the receipts by way of deductions from the purchase price were not in the nature of deposits. In this context, the reasoning of the Bench may be noticed.

"The essence of a deposit is that there must be a liability to return it to the party by whom or on whose behalf it is made on the fulfillment of certain conditions. Under the amended (sic unamended) by-law, the amounts deducted from the price and credited to the said fund were first liable to be used in adjusting the losses of the respondent-society in the working year; thereafter in the repayment of initial loan from the Industrial Finance Corporation of India and then for redeeming the Government share and only in the event of any balance being left, it was liable to be converted to share capital. The primary purpose for which the deposits were liable to be used were not to issue shares to the members from whose amounts the deductions were made but for the discharging of liabilities of the respondent-society. In these circumstances, the receipts constituted by these deductions were really trading receipts of the assessee society."

30. Although the use of the expression 'deposit' does not conclude the issue, there are intrinsic indications in the bye-laws that the expression has been used to mean just what it says. These are: (a) conversion of the deposit into additional shares, (b) transferability/heritability, (c) refundability, and (d) payment of interest on the deposit. The first three features are no doubt dependent upon occurrence of certain contingencies or hedged in by certain limitations. But the deposited amount is not denuded of its character of 'deposit' for that reason alone.

31. First, discussion needs to be focused on the first feature, namely, conversion of deposit into shares. The Tribunal rightly pointed out and it is not disputed before us that such conversion is as good as refund. Such conversion into additional shares is, however, postponed till the events of repayment of loans towards capital expenditure and the repayment of Government share capital happen. In other words, till such time, the member/depositor has no immediate right to demand the payment. Nevertheless, the obligation to repay stood annexed to the deposited amount at the time it was received by the assessee subject of course to the occurrence of the contingency specified in the bye-law itself. It cannot be said, as has been said by the High Court, that "under the bye-laws, no event or contingency has been contemplated" under which the members could demand the repayment of the deposit. Nor can it be said that even after the happening of the event specified in the bye-laws, the right to demand repayment becomes illusory in view of the discretion reserved to the Board of Directors of the Society.

In this context, much of the argument has been built up on the use of the expression 'may' followed by the words "convert such deposits into shares after payment of loans etc." It is contended by the learned counsel appearing for the Revenue that the Board of Directors may very well refuse to convert the deposits into shares in exercise of its discretion on the ostensible ground that the financial position of the Society does not permit such conversion. The very existence of discretion, it is pointed out, negates the existence of liability to convert the deposit into shares. We cannot accede to this contention. Once the loans of the description mentioned in the bye-laws which were outstanding on the date the deposit was made are repaid, in our view, the Board of Directors is bound to convert the deposit amount into shares. The discretion is always coupled with a duty; the discretion cannot be used to circumvent the obligation cast under the law or contract governing the parties. In our view, it would be appropriate to read the expression 'may' as 'shall'. On the occurrence of the specified event, namely, the repayment of the loans referred to in the bye-law and the Government share capital, the member/depositor can clutch at a legally enforceable right to demand repayment, may be, in the form of conversion into additional shares.

32. In our view, the retention of the deposited money with the Society in order to utilize the same for repayment of term loans etc., does not denude the amount of its character of 'deposit' carrying with it the obligation to repay. Nor is it necessary, as the High Court was inclined to think, that the separate identity of the deposited amounts should be kept up. The absence of the right to secure repayment on demand is again not inconsistent with the receipt being a deposit. Liability to return need not be immediate and unconditional, following a demand by the depositor. Even if such liability gets crystallized on the happening of a specified contingency, it is still a liability which can be legally enforced by the depositor. The existence of such liability is an antithesis to the idea of ownership of the money by the Society."

In the aforesaid decision the Hon'ble Supreme Court has further observed that the existence of other features such as transferability of the deposit to another member and the provision for refund of the deposited amount to the member in case of cessation of membership or to his legal heirs in case of death, are important indicators against the treatment of the deposited amount as the money belonging to the Society.

In the case before the Hon'ble Supreme Court it was also found that the deposited amount is not kept aside and even the same is used by the society for repayment of the loan and it was found that time of repayment is indefinite, however it was refundable on the occurrence of the contingencies specified in the bye-laws. To the aforesaid the Hon'ble Supreme Court has held that same does not denude the amount of its "character of deposit" carrying with it the obligation to repay and therefore, the Hon'ble Supreme Court did not accept the case of the Revenue that it may be treated as revenue income. In the aforesaid decision the Hon'ble Supreme Court distinguished the decision of the Hon'ble Supreme Court in the case of Bazpur Co-op Sugar Factory Ltd. (Supra). In para 26, the Hon'ble Supreme Court distinguished the decision of the Hon'ble Supreme Court in the case of Bazpur Co-op Sugar Factory Ltd. (Supra) by observing in para 26 as under:

"26. To what extent the principle laid down or the test applied in the Bazpur case can be pressed into service in the present case is the question which needs our close attention. There are two distinguishing features which become apparent on a reading of the bye-laws. The first is the absence of provision for payment of interest under the bye-laws of Bazpur Co-operative Sugars Ltd. Secondly, in Bazpur case the deducted amounts credited to "loss equalization and capital redemption reserve fund" are liable to be adjusted against the losses of any working year. It is only after adjusting such losses, the deposits are allowed to accumulate and be utilized for repayment of IFCI loan and for redeeming the Government's share contribution. In the process of such adjustment, the entire amount collected from the members and credited to the fund may be dissipated or consumed, whereas in the instant case, the amount collected as deposit remains intact, though it could be utilized from time to time for meeting certain liabilities of capital nature. However, there is one qualification in this behalf. If the society has not incurred any loss and it remains a profit-making concern, the situation will be very similar in both the cases. The amounts will then be utilized for repayment of long-term loans due to the financial institutions and the Government's share capital and after such process of repayment is complete, the disputed amounts could be made available to the grower members in the form of increased shares. Yet, in Bazpur case, at the time the sums were received from the grower-member and remitted to the loss equalization fund, there was no knowing whether the 'deposit' would

remain intact at all. The claim of the member to the deposited amount at that stage was too tenuous and slippery to earn the legal recognition of any proprietary interest over it. It cannot be said that the member had the right to get back the amount when it was recovered and credited to the Fund. The ultimate conclusion reached in Bazpur case can be explained on this basis. There is yet another angle from which the problem can be viewed. As between the member and the society, who is having substantial dominion over the 'deposits'? In Bazpur case the answer could only be that it is the assessee-society which had such dominion. The position is different in the present case, as explained hereafter.”

[8.6] Applying the above test to the present case and considering the fact that the security deposit is refundable after a period of 25 years or on occurrence of the contingencies mentioned in the bye-laws and it cannot be said that the assessee club had absolute dominion over the impugned deposits, the case on behalf of the Revenue that the same be treated as revenue income cannot be accepted. Merely because the security deposit is not kept apart and/or subsequently the amount of security deposit is utilized by the club for other purposes such as construction and providing other amenities at the club, the same shall not lose the “character of deposit”, which as observed hereinabove is refundable on occurrence of the contingencies as mentioned in the bye-laws. No error has been committed by the learned Tribunal in holding the same as Capital Receipt in view of the decision of the Hon’ble Supreme Court in the case of S.S. Sakhar Karkhana Ltd. (Supra).

[8.7] Now, so far as the decision of this Court in the case of Unique Mercantile Services Pvt. Ltd. (Supra) is concerned, it is required to be noted that infact before the Division Bench it was the case of fees and the question was whether the fees collected and recovered is required to be spread over in the span of 15 years and/or the same is required to be considered in the first year. In the case before the High Court as such there was no question as to whether such refundable security deposit

shall be treated as an income or not.

[9.0] In view of the above and for the reasons stated above and considering the fact that the security deposit recovered from the members at the time of their enrollment as a club member is refundable on occurrence of the contingencies mentioned in the Rules, Regulations and Bye-Laws, same is required to be treated as a deposit and therefore, the same is required to be considered as capital receipts. We confirm the impugned judgment and order passed by the learned Tribunal. The substantial question of law raised in the present appeals is answered in favour of the assessee and against the Revenue. Present Tax Appeals stand disposed of accordingly. No costs.

Sd/-
(M.R. SHAH, J.)

Sd/-
(B.N. KARIA, J.)

Ajay

