SYNOPSIS:

REVENUE'S ARGUMENTS:

They have supported the order of the Chief Commissioner of Income Tax and argued that no exemption under Section 10(23C)(vi) of the Act would be available to the petitioner because it is a Society registered under the 1860 Act and would not fall within the ambit of expression 'other educational institutions' as used in Section 10(23C)(iv) of the Act. Referring to the written statement filed on behalf of the respondents it has been submitted that once the educational society like the petitioner is accumulating systematic profits then it would not qualify to avail exemption in terms of Section 10(23C) (iv) of the Act. In that regard reliance has been placed on the Division Bench judgment of Uttrakhand High Court rendered in M/s Queens Educational Society's case (supra). According to the learned counsel the Division Bench of the Uttrakhand High Court has rightly taken the view that accumulation of surpluses year after year would necessarily result in shedding of character of an educational institution existing solely for education and then it would become a trading activity. It has been submitted that in order to continue with the character of an educational institution within the meaning of Section 10(23C)(iv) of the Act, the petitioner was required to stop accumulation of excesses by reducing the fees.

Assessee's Arguments:

As per the provisions of Section 10 (23C)(vi) read with the third proviso thereof, the capital expenditure, if incurred by the petitioner-society for the attainment of the objects of the society, has to be deducted from its gross receipts/income. This is so because the third proviso contains the expression 'applies its income, or accumulates it for application or, wholly and exclusively to the objects for which it is established'. The expression 'wholly' refers to the quantum of expenditure, whereas the expression 'exclusively' refers to the motive, object or the purpose of expenditure. It has been urged that the petitioner-society, when admittedly having utilized more than 100% of the income for achieving its objects could by no stretch of imagination, be held to be an educational institution existing for the purposes of making profit so as not to be entitled to exemption in view of the provisions of Section 10(23C) (vi) of the Act.

It has been submitted that the conclusion arrived at on the material and evidence on record by the Chief Commissioner of Income Tax while withdrawing exemption when viewed in the light of the principles and tests laid down by Hon'ble the Supreme Court it becomes unsustainable. He has argued that there are two reasons for the aforesaid view. Firstly, it has not been disputed by the Chief Commissioner that the petitioner-society exists solely for educational purposes. Secondly, even if there is any substantial profit resulting in surplus with the petitioner-society the institution would not cease to be not existing solely for educational purposes, inasmuch as, surplus/deficit is not determinative of the question as to whether the petitioner-society exists for making profit. Thus, the findings recorded by the Chief Commissioner would have no bearing which attract the

grounds of withdrawal laid down in American Hotel and Lodging Association's case (supra), especially when he observed that if substantial profits are earned in one year it would be the duty of the institution to lower its fees for the subsequent year so that such profits are not intentionally generated and if profits continue year after year then it could not be said that surplus is arising incidentally. Such reasoning is wholly irrelevant, inasmuch as, even if there is substantial surplus the institution can not cease to be one existing solely for educational purposes.

Learned counsel have substantiated their arguments by submitting that the Uttrakhand High Court has not appreciated correctly the ratio of the judgments of Hon'ble the Supreme Court in the cases of Aditanar Educational Institution (supra) and Children Book Trust (supra) and 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(23C) of the Act. It does not take the correct view of the judgment of Hon'ble the Supreme Court rendered in the case of American Hotel & Lodging Association Educational Institute (supra). According to the learned counsel, in principle the judgment of Uttrakhand High Court is in direct conflict with the decision rendered by the High Court of Allahabad in the case of City Montessori School v. Union of India and Others, (decided on 29th of May, 2009). Learned counsel has also apprised the Court that the Special Leave Petition preferred against the decision in City Montessori School's case, has been dismissed by Hon'ble the Supreme Court. 4.11 It has been further submitted that the Uttrakhand High Court has decided the controversy arising from the regular assessment proceedings which had emerged as a result of disallowance of capital expenditure thereby treating it as profit of the assessee at the hands of the Assessing Officer within whose jurisdiction the question of allow-ability of such an expenditure had arisen, though the genuineness of the existence of the Trust was not doubted.

High Court Order: & REASONING

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 deciding factor to conclude that the educational institution exists for profit.
(2) The provisions of Section 10(23C)(vi) of the Act are analogues to the erstwhile Section 10(22) of the Act, as has been laid down by Hon'ble the Supreme Court in the case of American Hotel and Lodging Association (supra). To decide the entitlement of an institution for exemption under Section 10(23C)(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 5-Judges Constitution Bench judgment in the case of Surat Art Silk Cloth Manufacturers Association (supra)]. 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 Hon'ble the Supreme Court in para 33 of its judgment in American Hotel and Lodging Association's case (supra). Thus, on an application made by an institution, the prescribed authority can grant approval subject to such terms and conditions as it may deems 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 of 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 (23C)(vi) of the Act. [See para 8.7 of the judgment – Aditanar Educational Institution case (supra)]

(5) Where more than 15% of income of an educational institution is accumulated on or after 01.04.2002, 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 Uttrakhand High Court rendered in the case of M/s Queens Educational Society (supra) and the connected matters, is not applicable to cases fall within the provisions of Section 10(23C)(vi) of the Act. There are various reasons, which have been discussed in para 8.8 of the judgment, and the judgment of Allahabad High Court rendered in the case of City Montessori School (supra) lays down the correct law.

## DISSENT WORDS FROM UTTARAKHAND HIGH COURT: MASS RELIEF PROVIDED TO EDUCATIONAL INSTITUTIONS

*We have not been able to persuade ourselves to accept the view expressed by the Division Bench of the Uttrakhand High Court in the case of M/s Queens Educational Society (supra). 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 Uttrakhand High Court pertained to Section 10(23C)(iiiad) of the Act. The third proviso to Section 10(23C)(vi) is not applicable to the cases falling within the purview of Section 10(23C)(iiiad). Secondly, the judgment rendered by the Uttrakhand High Court runs contrary to the provisions of Section 10(23C)(vi) of the Act including the provisos thereunder. Section 19(23C)(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(23C) of the Act [See observations in American Hotel and Lodging Association Educational Institute's case (supra)]. Thirdly, the Uttrakhand High Court has not appreciated correctly the ratio of the judgment rendered by Hon'ble the Supreme Court in the case of Aditanar Educational Institution (supra) and while applying the said judgment including the judgment which had been rendered by Hon'ble the Supreme Court in the case of Children Book Trust (supra), 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(23C) of the Act. Lastly, that view is not consistent with the law laid down by Hon'ble the Supreme Court in American Hotel & Lodging Association Educational Institute (supra).*