

(1991) 04 AHC CK 0052

In the Allahabad High Court

Case No : Income-tax Reference No. 229 of 1981

Commissioner of Income Tax

APPELLANT

Vs

J.K. Charitable Trust

RESPONDENT

Date of Decision : 09-04-1991

Acts Referred:

Income Tax Act, 1961 — Section 11, 11(3), 13(2), 144A, 144B

Citation : (1992) 196 ITR 31

Hon'ble Judges : B.P. Jeevan Reddy, C.J;S.R. Singh, J

Bench : Division Bench

Final Decision : Disposed Of

Judgement

B.P. Jeevan Reddy, C.J.—In this reference made u/s 256(1) of the Income Tax Act, 1961, as many as eleven questions are stated, eight at the instance of the Revenue and three at the instance of the assessee. The questions referred at the instance of the Revenue are :

"1. Whether, on the facts and in the circumstances of the case and on the input of the provisions of Sections 144A and 144B of the Income Tax Act, 1961, the Inspecting Assistant Commissioner was not competent to give directions to the Income Tax Officer in the manner he did ?

2. Whether, on the facts and in the circumstances of the case, the object Clause 2(h) of the deed of trust dated January 24,1944, is of charitable nature ?

3. Whether, on the facts and in the circumstances of the case, the donations made to other charitable trusts would be hit by the provisions of Section 11(3) of the Income Tax Act, 1961 ?

4. Whether, on the facts and in the circumstances of the case, the authors of the trust and/or its trustees had substantial interest in M/s J. K. Commercial Corporation ?

5. Whether, on the facts and in the circumstances of the case, the interest/rent

received by the assessee from various concerns was not adequate within the meaning of Section 13(2)(a) of the Income Tax Act, 1961 ?

6. Whether, on the facts and in the circumstances of the case, the shares of M/s. J. K. Synthetics Ltd. received by the assessee-trust in earlier years would not be hit by the provisions of Section 13(2)(h) of the Income Tax Act, 1961 ?

7. Whether, on the facts and in the circumstances of the case, the transactions carried on by the assessee in shares would disentitle the assessee from being treated as a charitable institution within the meaning of Section 2(15) of the Income Tax Act, 1961 ?

8. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that there is no mistake apparent on the face of the record in its order dated September 27, 1977 ?"

2. The three questions referred at the instance of the assessee read thus :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal erred in law in not adjudicating upon the issues as specifically raised and pleaded on behalf of the assessee-trust regarding the lack of jurisdiction of the Income Tax Officer in considering three new issues during the reassessment proceedings, although the said issues were neither considered in the relevant original assessment nor were the subject-matter of directions by the appellate authority, while setting aside the original assessment ?

2. Whether, on the facts and in the circumstances of the case and having regard to the relevant directions contained in the appellate order remanding the assessment proceedings to the Income Tax Officer, the Income Tax Officer exceeded his jurisdiction in considering and adjudicating upon three new issues relating to the eligibility of the trust for exemption, although the said issues were neither considered in the relevant original assessment nor were the subject-matter of directions by the appellate authority while setting aside the said original assessment ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that the second proviso to section 13(1)(c) of the Income Tax Act, 1961, did not save the transactions for use of application of funds made before June 1, 1979, from the disability arising u/s 13(2)(h) of the said Act ?"

3. The assessee is a trust. The assessment years concerned are 1972-73 and 1973-74. Calendar years 1971 and 1972 were, respectively, the previous years.

4. The assessee-trust was created by an instrument of trust executed on January 24, 1944. The assessee claims to be a religious and charitable trust. The objects of the trust are found in Clause 2 of the deed of trust. It reads thus :

"(a) The construction of temples, dharmashalas and chatrams, wells, school building's and buildings or structures of similar nature whether temporary or

permanent and making provision for their equipment, upkeep and maintenance.

(b) The promotion of education of poor and deserving students including grant of prizes, scholarships, studentship to students of any school, college or other institutions.

(c) Construction and/or establishment of schools, colleges, and/or other educational institutions, hostels for students and making provision for their equipment, upkeep and maintenance.

(d) Grant-in-aid to schools, colleges and/or educational institutions.

(e) To bind as apprentices to any profession, trade, industry or manufacture, poor and deserving youths on payment of such minimum and on such terms and conditions as the trustees may deem fit.

(f) To give loans to poor and deserving students to enable them to prosecute their studies in Europe, America, India or elsewhere in such subjects and for such period as the trustees may think fit and on such terms as to repayment of the loan in such installments, at such rate of interest or without interest or otherwise and subject to such provisions and conditions as the trustees may deem fit.

(g) To establish, erect, fit up and furnish one or more polytechnic institute or institutes for the training of young men in technical, mechanical, scientific and other pursuits as the trustees may determine and to make provision for their upkeep and maintenance.

(h) The establishment, equipment, upkeep and maintenance of industrial homes for men as well as women out of employment for teaching them all such arts, handicrafts and home industries including carpentry, jointly designing, drawing, painting, cane-work, carpet making spinning, weaving, laundry work, dry-cleaning, cooking, confectionery, knitting, sewing, embroidery and such other industries as the trustees may deem fit and making provision for payment to them daily, weekly or monthly such wages or remuneration according to place, work or otherwise as the trustees may determine.

(i) Provision of medical relief for the poor including the construction, equipment, upkeep and maintenance of dispensaries and hospitals, including maternity hospitals for the poor and free ante-natal and post-natal or other medical help or advice and treatment as the trustees may determine.

(j) The establishment, upkeep and maintenance of rent-free homes for poor and incapacitated persons, the supply of necessities to the poor and the incapacitated, giving of alms to them and for their general benefit as the trustees may from time to time determine.

(k) And generally for the benefit of the poor and the incapacitated and/or such deserving persons including the marriage of poor women and the advancement of any other object of general public utility as the trustees may in their absolute

discretion deem fit and in such way as they may consider most advantageous to the recipients."

5. For the assessment year 1972-73, the assessee filed a return declaring an income of Rs. 2,489.27. For the rest of the income, it claimed exemption u/s 11. The Income Tax Officer, however, added back several amounts under the provisions of Sections 11 to 13 and assessed the income at Rs. 2,54,670. The assessee filed an appeal which was allowed in part. The Appellate Assistant Commissioner remitted the matter to the Income Tax Officer with certain directions. The assessee carried the matter in further appeal to the Tribunal, which was allowed and the order of the Appellate Assistant Commissioner was set aside. The matter, however, was remitted to the Income Tax Officer. On this occasion, the Income Tax Officer prepared a draft of the proposed order of assessment as contemplated by Section 144B(1), invited the assessee's objections and forwarded the draft and the objections of the assessee to the Inspecting Assistant Commissioner. The Inspecting Assistant Commissioner heard the assessee and gave certain directions, in accordance with which the Income Tax Officer completed the assessment whereunder he determined the total income of the assessee at Rs. 8,61,690.

6. With respect to the assessment year 1973-74, the proceedings followed practically the same course. In these proceedings too, Section 144B was followed and assessment completed, determining the assessee's income at Rs. 36,50,739.

7. The assessee preferred appeals against both the assessment orders which were disposed of by a common order dated February 10, 1977, by the Appellate Assistant Commissioner allowing the appeals in part, which resulted in both the Revenue and the assessee filing appeals to the Tribunal. The Tribunal allowed the appeals preferred by the assessee and dismissed the appeals filed by the Revenue by its order dated September 27, 1977. Thereafter, an application for rectification was filed u/s 254(2) by the Revenue which was ultimately dismissed on December 22, 1979. It is then that both the Revenue and the assessee applied for and obtained this reference. We shall proceed to deal with each of the questions separately.

8. Question No. 1.--While narrating the facts, we have mentioned the fact that, with respect to both the assessment years, the Income Tax Officer followed the procedure prescribed by Section 144B. As required by the said section, he prepared a draft assessment order, invited the objections of the assessee and forwarded both of them to the Inspecting Assistant Commissioner. The Inspecting Assistant Commissioner heard the assessee and gave certain directions. While giving these directions, the Inspecting Assistant Commissioner appears to have opined that Clause 2(h) of the objectives of the trust cannot be said to be charitable. The objection of the assessee to this opinion was that it was beyond the purview of the draft assessment order and hence the Inspecting Assistant Commissioner acted beyond his powers in expressing the said opinion. The Revenue, however, relied upon the provisions contained in Section 144A to

sustain the said opinion or instructions as it may be called. The Tribunal agreed with the assessee that the Inspecting Assistant Commissioner had no jurisdiction to give any instructions which were beyond the purview of the draft assessment order and the objections filed by the assessee. In our opinion, the Tribunal was right.

9. Sub-section (4) of Section 144B reads as follows :

"144B.(4) If any objections are received the Income Tax Officer shall forward the draft order together with the objections to the Inspecting Assistant Commissioner and the Inspecting Assistant Commissioner shall, after considering the draft order and the objections and after going through (wherever necessary) the records relating to the draft order, issue, in respect of the matters covered by the objections, such directions as he thinks fit for (the guidance of the Income Tax Officer to enable him to complete the assessment.

Provided that no directions which are prejudicial to the assessee shall be issued under this sub-section before an opportunity is given to the assessee to be heard."

10. So far as reliance upon Section 144A is concerned, it undoubtedly conferred upon the Inspecting Assistant Commissioner power to call for and examine the record of any proceedings relating to a pending assessment and issue appropriate directions for the guidance of the Income Tax Officer. But, this is an independent power and if the Inspecting Assistant Commissioner wanted to invoke this power and give particular directions (with respect to the interpretation of Clause 2(h) of the objectives of the trust), he ought to have given the assessee a notice about it and heard it in that behalf before giving any such directions. Since he has not done that, the said opinion or instructions, as it may be called, cannot be sustained. Question No. 1 (referred at the instance of the Revenue) is, accordingly, answered in the affirmative, that is, in favour of the assessee and against the Revenue.

11. Question No. 2.-This question relates to the interpretation of Clause 2(h) of the deed of trust. We have already set out Clause 2. Clause 2(h) empowers the trustees to establish, equip and maintain industrial homes for teaching unemployed persons arts like handicraft and other home industries and to make provision for payment to them daily, weekly or monthly, such wages or remuneration as the trustees may determine on the basis of place, work or otherwise. The main idea underlying the clause is to impart training (teaching) in arts and handicrafts to unemployed men and women. No doubt, the clause provides for payment for such work, but, in the context, it must be understood as a payment in the nature of a stipend. It cannot be equated to regular wages nor can the said clause be understood as establishment of a regular unit engaged in business in the said arts and handicrafts. As rightly pointed out by the Tribunal, Clause 2(h) should not be read in isolation, but must be read along with other objects and interpreted having regard to the totality of the objects. The

second question is, accordingly, answered in the affirmative, that is, in favour of the assessee and against the Revenue.

12. Question No. 3 is the most important question which we shall take up after we deal with other questions.

13. Question No. 4.--This question raises the issue whether the authors of the trust and/or trustees had substantial interest in M/s. J. K. Commercial Corporation. The Tribunal has set out in detail the shareholding of each of the authors of the trust and/or the trustees and has found that their shareholding in J. K. Commercial Corporation is only 13 per cent. According to Explanation 3 to Section 13(4), the shareholding must be 20 per cent, to become a substantial holding. The Department's contention was that shares held by two other persons, Purshottam Dass Singhanian and Balakrishna Singhanian, for and on behalf of the assessee-trust should also be taken into account which was negated by the Appellate Assistant Commissioner and the Tribunal, and, in our opinion, rightly. This question is, accordingly, answered in the negative, that is, in favour of the assessee and against the Revenue.

14. Question No. 5.--This question arises with reference to Clause (a) of Sub-section (2) of Section 13. The issue is whether the interest/rent charged by the assessee-trust on loans advanced and buildings leased out to certain concerns are hit by the said provisions on the ground that the interest/ rent charged is not adequate. Our attention was invited to the loans advanced to three companies on interest at the rate of six per cent. The Revenue's contention was that any interest below nine per cent must be deemed to be inadequate. The Tribunal, however, found that they were secured loans though the rate of interest during the calendar year 1971 was six per cent, and during the calendar year 1972 interest paid by the borrowers was 7.5 per cent. Having regard to the facts of the case before them and the meagre difference between the interest actually charged and the interest which ought to have been charged, the Tribunal held that the interest charged was not inadequate. So far as the lease rent of the building is concerned, it is brought to our notice that the property called Kamla Castle, Mussorie, was leased out at a meagre rent of Rs. 1,250 per month. It was submitted that it is a big bungalow at an important hill station and, therefore, the rent stipulated must be deemed to be inadequate. The Tribunal, however, pointed out that this property was donated by Sir Padampat Singhanian in the "previous year" relevant to the assessment year 1971-72 and its value, as per the balance-sheet, was Rs. 2,86,347. The Tribunal also took into consideration the fact that properties in hill stations do not fetch income throughout the year but only during the tourist season. Accordingly, it held that the rent charged cannot be said to be inadequate. We are unable to see that this finding is open to objection in any manner. Question No. 5 is, accordingly, answered in the negative, that is, in favour of the assessee and against the Revenue.

15. Question No. 6.--It appears that certain shares of J. K. Synthetics Ltd. were donated to the assessee-trust. They were 40,000 in number. J. K. Synthetics Ltd.

appears to have issued bonus shares, 20,000 in number. The Income Tax Officer was of the opinion that the value of the bonus shares should be deemed to be an investment and as J. K. Synthetics Ltd. was controlled by the authors of the assessee-trust, the transactions fell within the mischief of Section 13(2)(h) of the Act. This view of the Income Tax Officer was repelled by the Tribunal and here again we agree with it. The issuance of bonus shares cannot be treated as an investment by the assessee-trust. It is not suggested that it was a bogus plea or that it was not a bona fide transaction. Question No. 6 is, accordingly, answered in the negative, that is, in favour of the assessee and against the Revenue.

16. Question No. 7.--It was found by the Tribunal that a few dealings in shares entered into by the assessee were not by way of business, but it was only a case of change of investment as would have been done by any other wise and prudent person. This finding of the Tribunal has not been seriously challenged before us and we accept the same. In this view of the matter, it is unnecessary for us to consider whether the trust ceased to be a religious/charitable trust in case it carries on business. Question No. 7 is, accordingly, answered in the negative, that is, in favour of the assessee and against the Revenue.

17. Question No. 8.--This question relates to the correctness of the order passed by the Tribunal on the rectification application. The final order passed by the Tribunal, following the opinion of the third member, has not been challenged before us by learned standing counsel for the Revenue. Accordingly, we answer question No. 8 in the affirmative, that is, in favour of the assessee and against the Revenue.

18. So far as the three questions referred at the instance of the assessee are concerned, it is conceded before us by learned counsel for the assessee that these questions raised minor issues and need not be gone into by us. Accordingly, we decline to answer these three questions.

19. We shall now take up question No. 3 referred at the instance of the Revenue which was the main question canvassed before us. Before we take up the question proper, it would be appropriate to briefly notice the relevant provisions of the Act as they stood at the relevant time. Section 11(1) provided, inter alia, that income derived from property held under trust wholly for charitable or religious purposes shall not be included in the total income to the extent to which the said income is applied to charitable/religious purposes in India. Sub-section (2) of Section 11 provided that even if the income is not so applied but is accumulated or set apart for application to such purposes in India, even then it shall be exempt, provided certain conditions specified in the sub-section are complied with. Sub-section (3) of Section 11 then said that in case any income referred to in Sub-section (2) is applied to purposes other than charitable or religious purposes or ceases to be accumulated or set apart for application to such purposes, it shall cease to be exempt and shall be included in the income of the previous years in which it is so applied for other purposes or ceases to be accumulated or set apart for application to such purposes. Section 12, as it

obtained prior to April 1, 1973, contained two sub-sections. Under Sub-section (1), any income of a trust created for charitable/religious purposes, derived from voluntary contributions and applicable solely to charitable or religious purposes, shall be exempt. Sub-section (2) dealt with a case where charitable/religious trust received contributions from another religious/charitable trust to which Section 11 applied. The sub-section said that such contributions shall, in the hands of the recipient-trust, be deemed to be income derived from property for the purposes of Section 11 and all the provisions of Section 11 shall apply accordingly. It would be appropriate to set out Section 12 in its entirety as it obtained prior to April 1, 1973 :

"12. (1) Any income of a trust for charitable or religious purposes or of a charitable or religious institution derived from voluntary contributions and applicable solely to charitable or religious purposes shall not be included in the total income of the trustees or the institution, as the case may be.

(2) Notwithstanding anything contained in Sub-section (1), where any such contributions as are referred to in Sub-section (1) are made to a trust or a charitable or religious institution by a trust or a charitable or religious institution to which the provisions of Section 11 apply, such contributions shall, in the hands of the trust or institution receiving the contributions, be deemed to be income derived from property for the purposes of that section and the provisions of that section shall apply accordingly."

20. Section 12 was substituted in its entirety by the Finance Act, 1972, with effect from April 1, 1973. The substituted Section 12 reads as follows :

"12. Any voluntary contributions received by a trust created wholly for charitable or religious purposes or by an institution established wholly for such purposes (not being contributions made with a specific direction that they shall form part of the corpus of the trust or institution) shall for the purposes of Section 11 be deemed to be income derived from property held under trust wholly for charitable or religious purposes and the provisions of that section and Section 13 shall apply accordingly."

21. Section 13 provided situations where the exemption provided by Sections 11 and 12 shall not apply. The several provisions of Section 13 are designed to ensure the religious/charitable nature of the trust and to ensure further that its functioning does not result in any benefit to the authors of the trust or relatives or concerns controlled by them.

22. Now, the question is whether the donations made by the assessee-trust to other charitable trusts are hit by Section 11(3) of the Act. For the sake of convenience, we may set out Sub-section (3) in full. It reads :

"(3) Any income referred to in Sub-section (1) or Sub-section (2) as is applied to purposes other than charitable or religious purposes as aforesaid or ceases to be accumulated or set apart for application thereto or is not utilised for the purpose

for which it is so accumulated in the year immediately following the expiry of the period allowed in this behalf shall be deemed to be the income of such person of the previous year in which it is so applied, or ceases to be so accumulated or so set apart or, as the case may be, of the previous year immediately following the expiry of the period aforesaid."

23. The Tribunal was of the opinion that contribution to other charitable trusts is within the power and competence of the trustees. It has relied upon Sub-clause (k) of Clause 2 of the deed of trust which, inter alia, empowers the trustees to apply the income of the trust for "the advancement of any other object of general public utility as the trustees may in their absolute discretion deem fit and in such way as they may consider most advantageous to the recipients." We are inclined to agree with it. A charitable purpose may be served in more than one way. One is to directly contribute for the promotion of that cause ; the other is to contribute money to another charitable organisation, which advances that cause. In the absence of allegations of device and or mala fides, the amount contributed to other charitable institutions out of the income accumulated under Sub-section (2) is outside the mischief of Sub-section (3) of Section 11. In other words, such contribution does not amount to application of the income for purposes other than charitable or religious purposes.

24. A good amount of controversy, however, raged as to the position where such contributions are made, not out of the income accumulated under Sub-section (2), but out of contributions received by the assessee-trust. We have already set out Section 12 as it obtained prior to April 1, 1973, and also as it obtains with effect from the said date. Out of the two assessment years, the assessment year 1972-73 is governed by the unamended Section 12, whereas the assessment year 1973-74 is governed by the amended Section 12. The change in Section 12, however, makes no difference in so far as the facts of the present case are concerned. u/s 12(1) as it stood prior to April 1, 1973, the income of a charitable/religious trust, derived from voluntary contributions and applicable solely to charitable/religious purposes was not liable to be included in the total income of the trust or the trustees as the case may be. It is not the case of the Revenue that the contributions were made to the assessee-trust with a direction to apply them to purposes other than charitable or religious ; evidently, the persons/organisations contributing the amounts to the assessee-trust intended them to be applied to charitable or religious purposes. Once we hold that contribution to another charitable trust is an application for charitable purposes, no further question arises. In other words, such contribution to another charitable trust by the assessee-trust cannot be treated as the income of the assessee-trust in the year of contribution. Even if we apply Section 12 as it obtains from April 1, 1973, and applicable to the assessment year 1973-74, the result is not different. According to the amended Section 12, voluntary contributions received by a religious/charitable trust shall, for purposes of Section 11, be deemed to be income derived from property held under trust wholly for charitable/religious purposes and the provisions of Sections 11 and 13 shall apply accordingly.

Therefore, so far as the assessment year 1973-74 is concerned, the position (with respect to the amounts contributed by the assessee-trust to other charitable-trust from out of contributions received by it) is the same as the one obtaining with respect to income derived by the assessee-trust from the properties held under trust wholly for charitable or religious purposes.

25. An incidental issue was also debated before us. It was contended by learned counsel for the assessee that the amended Section 12 does not apply to the assessment year 1973-74 and that it applies to and with effect from the assessment year 1974-75. It is not possible to agree. Section 12 was amended (substituted) by the Finance Act, 1972, with effect from April 1, 1973. The contention of learned counsel was that the said section applies only to the financial year 1973-74, which would mean the assessment year 1974-75, but not to the assessment year 1972-73, for which the "previous year", in the case of the assessee, happens to be the calendar year 1972. His contention was that since Section 12 has been substituted with effect from a date subsequent to the expiry of the assessee's previous year, it does not apply to it. We are unable to appreciate this argument. The unit for applying the Act is the assessment year. Until recently, the previous years differed from assessee to assessee. It could be the preceding financial year or any other period of 12 months ending on any date in the previous financial year. That this is so is made clear by several decisions including *Reliance Jute and Industries Ltd. Vs. Commissioner of Income Tax, West Bengal*, *Commissioner of Income Tax, West Bengal Vs. Isthmian Steamship Lines*, and other decisions collated at page 110 of Kanga and Palkhivala's *The Law and Practice of Income Tax*, 8th edition, Volume 1. We do not think it necessary to reiterate all the decisions on this question inasmuch as we have held that whether it is the unamended Section 12 or the amended Section 12, the question must be answered in favour of the assessee.

26. For the above reasons, question No. 3 is answered in the negative, that is, in favour of the assessee and against the Revenue.

27. The reference is disposed of accordingly. There shall be no order as to costs.