

IN THE INCOME TAX APPELLATE TRIBUNAL
“SMC” BENCH : BANGALORE

BEFORE SHRI D. MANMOHAN, VICE PRESIDENT

ITA No.664/Bang/2015
Assessment year : 2011-12

Public Education Society, C/o. St. Mira's High School, No.201, 6 th Block, Rajajinagar, Bangalore – 560 010. PAN : AABTP 1260A	Vs.	The Deputy Director of Income Tax (Exemptions), Circle 17(2), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri P. Prathik, C.A.
Respondent by	:	Shri P.K. Sreehari, Addl. CIT(DR)

Date of hearing	:	25.08.2015
Date of Pronouncement	:	25.08.2015

ORDER

This appeal by the assessee is directed against the order dated 30.01.2015 passed by the CIT(Appeals)-14, Large Taxpayers Unit, Bangalore and pertains to assessment year 2011-12.

2. The assessee is an educational society and it obtained registration under the provisions of section 12A of the I.T. Act vide registration dated

27.5.2009. For the year under consideration, it filed its return of income wherein NIL income was declared after giving effect to provisions of section 11 of the Act.

3. The case was taken up for scrutiny. The Assessing Officer noticed that the assessee received gross amount of Rs.2,96,29,585 in the form of tuition fees from students, interest on deposits and miscellaneous income. Out of the said receipts, a sum of Rs.2,39,10,198 was applied towards objects of the society in the form of salaries to teachers and staff and other administrative expenses, excluding depreciation. The assessee has also applied a sum of Rs.38,75,370 towards acquisition of fixed assets. The total expenditure incurred by the assessee with reference to gross amount received shows that the assessee society applied the funds to the tune of 93.77% and the balance 6.23% was accumulated out of the gross funds received. Since it is within the permissible limits of accumulation contained in section 11(1)(a) of the Act, according to assessee, no tax was payable for the assessment year under consideration.

4. The Assessing Officer was, however, of the opinion that gross receipts of educational institution should not be taken into consideration since as per the commercial principles, the expenditure incurred for running the activities of the trust have to be reduced from gross receipts and from the balance amount, it has to be seen as to what is the percentage of income that was applied for charitable activities. From this perspective, the

assessee cannot be said to have applied more than 85% for charitable activities. In other words, the surplus available with educational institution is more than 15%. The AO also observed that gross receipts can be taken into consideration only when the entire receipts are in the form of donations since an assessee need not spend anything on getting donations, whereas in the case of an educational institution, the assessee has to bear the revenue expenditure for earning the income in which event, only the net income has to be taken by applying commercial principles. Though the assessee relied upon the decision of the Hon'ble Kerala High Court in *Programme for Community Organisation, 228 ITR 620 (Ker)*, which was affirmed by the Hon'ble Supreme Court in *240 ITR 1 (SC)*, the AO was of the view that the said case law is applicable only in respect of amount received in the form of donations and not the amount received by carrying on the activity such as imparting education. As per the computation of the AO, the balance amount works out to Rs.57,19,387, out of which the assessee has incurred capital expenditure of Rs.38,75,380 and, to the extent of 15%, which works out to Rs.8,57,908 the assessee is entitled to accumulate/set apart for application for charitable purposes u/s. 11(1)(a) and the balance was treated as taxable income.

5. In appeal filed by the assessee, the Id. CIT(Appeals) has adopted the same view and thus, the assessee is in appeal before the Tribunal.

6. At the time of hearing, the Id. counsel for the assessee submitted that the Circular issued by CBDT dated 19.6.1968, no doubt, speaks of the ambit of the expression "income", but it has no application in this context inasmuch as the provisions of section 11(1)(a) uses the expression "such income", which in turn refers to gross income. In this regard, he filed detailed written submissions which are reproduced below for the sake of convenience:-

“9. It is also stated by the learned Commissioner that there is nothing in the Circular to indicate that even revenue expenditure should be added back in the case of charitable or religious trusts running educational institutions or hospitals. Effectively, it is stated that revenue expenditure incurred by educational institutions does not constitute “applications thereof towards the purposes of the Trust” as clarified by the Circular, a view which runs counter to the ratio of the decision of the Calcutta High Court in CIT vs. Birla Janahit Trust (208 ITR 372) where their Lordships held as follows:

“In our view, therefore, the expenditure on salaries and miscellaneous expenses for the purpose of carrying out the objects and purposes of the trust must be considered as application for charitable purposes. However, in this case the quantum of the expenditure for carrying out the objects and purposes of the trust and the expenditure made to earn the income had not been separately allocated or determined. We, therefore, answer the second question by saying that the Tribunal was right in holding that the assessee will be entitled to the benefit of the expenditure made on salaries and miscellaneous expenses for the purpose of carrying out the objects and purposes of the trust only; but any expenditure incurred for earning the income from dividend will not qualify as amounts spent for carrying out the objects and purposes of the trust.”

The said decision was cited during the course of the appellate proceedings, but the learned Commissioner has refused to accept the same alleging that though the decision was rendered in favour of the assessee, the reason given by the bench was that the said expenses had been earned not only for the dividend income earned but also for the other purposes of the Trust. Your Lordships will readily appreciate that the slight inconsequential difference in the facts governing this case will not alter the applicability of the ratio of the said judgement to this case. All the expenditure incurred by the appellant was for the purposes of the objects of the Trust, and no fault has been found with that. That whether the activities of the Trust are charitable in nature has also not been questioned or doubted by either the learned Commissioner or the assessing officer. Nothing could therefore be more appropriate than to regard the expenditure incurred by the Trust as having been incurred for charitable purposes.

10. The decision of the Hon'ble Supreme Court in the case of CIT vs. Programme for Community Organisation [248 ITR 1] which while dealing with the issue, had held that a charitable or religious trust is entitled to accumulate twenty-five per cent of its gross income derived from property held under trust, was also brought to the attention of the learned CIT(Appeals). There, their Lordships had elucidated their view by stating that the limit of 25% (as applicable then) was to be construed with reference to the gross donations received by the Trust and not the net sum available after the application from out of such donations. But this decision was also distinguished by the learned Commissioner on the grounds that such decision was rendered only the context of a trust or institution running purely on donations and will therefore not apply to an educational institution which accepted fees and had to incur expenses to earn such fees. It is submitted that there is nothing in the aforesaid decision of the Hon'ble Supreme Court to suggest that it is applicable only to a Trust or institution running purely on donations, and not in the case of any other charitable institution in receipt of any other income. The learned Commissioner has reiterated the view of the assessing officer that whereas it is well settled that no expenditure is required to be incurred in order to earn donations, running of an educational institution requires the administrative expenses to be incurred in order to earn the income, and therefore it is only the net surplus available after deduction of all expenses, if at all, that has to be considered in computing the permissible accumulation.

11. The Hon'ble Lucknow Bench of the Income-tax Appellate Tribunal in the case of Krishi Utpadan Mandi Samithi [131 ITD 335] while dealing with an appellant who was in receipt of income other than donations, and which had to incur administrative expenses for its functioning, has held in unequivocal terms that the ratio laid down by the Apex Court in 248 ITR 1 (supra) is applicable to the case, and that the appellant was entitled to accumulate 15 percent of its gross receipts and not 15% of the income worked out for tax purposes. This has also been rejected by the learned Commissioner on grounds that there is no discussion on whether the source of the receipts were donations or some other source. The said ratio laid down by the Hon'ble Supreme Court was also interpreted by a Special Bench of the Bombay ITAT in Bai Sonabai Hirji Agiary Trust vs. Fifth Income-tax Officer [272 ITR (AT) 67], where on a combined reading of the judgement of the Hon'ble Supreme Court in the case of Programme for Community Organisation (supra) and the earlier decision in the case of the same appellant by the Hon'ble Kerala High Court, their Lordships opined as follows:

“... It has been held that as per the statutory language of the above section the income which is to be taken for the purpose of accumulation is the income derived by the trust from property. If both the decisions are carefully read, it becomes evident that any expenditure which is in the shape of application of income is not to be taken into account. Having found that the trust is entitled to exemption under section 11(1), we are to go to the stage of income before application thereof and take into account 25 per cent, of such income. Their Lordships have pointed that the same has to be taken on “commercial” basis and not “total income” as computed under the Income-tax Act. Their Lordships in the decided case rejected the contention of the Revenue that the sum of Rs. 1,70,369 which was spent and applied by the assessee for charitable purposes was required to be excluded for the purpose of taking amount to be accumulated. Having regard to the clear pronouncement of their Lordships of the Supreme Court it is difficult to accept that outgoings which are in the nature of application of income are to be excluded...” ”

7. In particular, the assessee placed reliance upon the ITAT Mumbai Special Bench in the case of *Bai Sonabai Hirji Agiary Trust* [272 ITR (AT) 67] wherein, on identical issue, the Tribunal observed as under:-

“From the above, it would appear that the dispute is limited to correct amount of income from house property, whether it should be gross rent of Rs.2,63,675 or the net income after deducting outgoings and depreciation.”

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“Shri V.H. Patil further submitted that the Kerala High Court (see [1997] 228 ITR 620), in the same case, has referred to the Board’s Circular dated June 19, 1968, on the same subject and observed that “income” for the purposes of section 11(1), should be understood in its commercial sense. It was held by the Kerala High Court that 25 per cent of gross amount of Rs. 2,57,376 should be accumulated, and this finding has been confirmed by the hon’ble Supreme Court. Shri V. H. Patil also contended that all out-goings including expenditure incurred by a public charitable trust must be considered to be in the nature of application of income for the objects and purposes of the trust. It is, therefore, contended that 25 per cent of the gross income as reflected in the account of the assessee-trust should be allowed to be accumulated under section 11(1).”

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“Having regard to the clear pronouncement of their Lordships of the Supreme Court it is difficult to accept that outgoings which are in the nature of application of income are to be excluded. The income available to the assessee before it was applied is directed to be taken and the same in the present case is Rs. 3,42,174. Twenty-five per cent of the above income is to be allowed as a deduction. Similar view has also been taken by the hon’ble Madhya Pradesh High Court in *Parsi Zoroastrian Anjuman Trust Mhow v. CIT* [1987] 163 ITR 832. No reason whatsoever has

been given by the revenue authorities for deducting Rs. 2,17,126 in this case for purposes of section 11(1)(a). The decision cited on behalf of the Revenue did not take into account the decision of the Supreme Court referred to above. The circular of the Central Board of Direct Taxes has also been considered by the hon'ble Kerala High Court in its decision referred to above. Accordingly, the question referred to us is answered in the affirmative and in favour of the assessee.”

8. The Id. DR, on the other hand, strongly relied upon the orders of tax authorities and contended that educational institutions are rendering an activity of profit and in those cases, expenditure incurred for earning income should first be deducted and only on the balance amount, it has to be seen as to whether the assessee has applied the same for charitable objects or not.

9. I have considered the rival submissions and perused the record. The issue herein is with regard to the meaning of expression “such income” in section 11(1)(a) of the Act. Identical issue was considered by the Apex Court (*supra*) which was also applied by the Special Bench of the ITAT Mumbai by holding that the expression “such income” means gross income and not the net income after deducting the administrative expenditure. Such being the case, by respectfully following the decision of the Special Bench, I hold that the claim of assessee is in accordance with law. Since the expenditure incurred by the assessee was more than 93% of the gross receipts, no part of the gross receipts are liable to be taxed in the year under consideration, since the balance amount was set apart for

application in the next year. With these observations, the appeal filed by the assessee-trust is allowed.

Pronounced in the open court on this 25th day of August, 2015.

Sd/-

(D. MANMOHAN)
Vice President

Bangalore,
Dated, the 25th August, 2015.

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Copy to:

1. Appellant
2. Respondents
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar
ITAT, Bangalore.