IN THE HIGH COURT OF JUDICATURE AT MADRAS

RESERVED ON : 04.3.2019 & 15.3.2019
DELIVERED ON: 20.3.2019

CORAM

THE HON'BLE DR.JUSTICE VINEET KOTHARI
AND
THE HON'BLE MR.JUSTICE C.V.KARTHIKEYAN

Writ Appeal Nos.391 to 402, 569 to 583, 585 to 596, 598, 599 & 603 of 2019 ***(Reserved on 04.3.2019)***
&
W.A.Nos.817, 819 to 827, 829, 832, 833, 837 to 844, 846, 836, 897 to 906 of 2019 ***(Reserved on 15.3.2019)***

W.A.No.391 of 2019

1. Union of India
   rep. by the Secretary
   Ministry of Finance
   North Block
   New Delhi 110 001.

2. Central Board of Direct Taxes
   rep. by the Secretary
   Ministry of Finance
   North Block
   New Delhi 110 001.

3. Principal Chief Commissioner of Income-tax (Chennai)
   121, MG Road
   Nungambakkam
   Chennai 600 034.

4. The Commissioner of Income-tax (TDS)
   7th Floor, New Block
   Aayakar Bhawan
   121, MG Road

Nungambakkam
Chennai 600 034. .. Appellant

Vs.

1. The Society of Mary Immaculate (Tamil Nadu)
rep. by its President
Mercy Home 64
Halls Road, Kilpauk
Madras 10.

2. Director of Treasuries and Accounts
Office of the Treasuries and Accounts
Panagal Building
No.1, Jeenis Road
Saidapet
Chennai 600 015.

3. The Director of School Education
DPI Campus
College Road
Chennai 600 006.

4. The Director of Elementary Education
DPI Campus
College Road
Chennai 600 006. .. Respondents

Appeal filed under Clause 15 of the Letters Patent against the common order dated 22.12.2016 made in W.P.Nos.38026 of 2015.

For Appellant	:	Mr.Karthik Ranganathan Standing Counsel
For Respondent-1 in all WAs, except WA Nos.573, 832, 833, 838, 840 & 841/19	:	Mr.Arvind Datar, S.C. Fr. Xavier Arulraj, S.C. Assisted by Ms.A.Arul Mary Fr. Xavier Associates

For Respondent-1 in Nos.573, 832, 833, 838, 840 & 841/19 : Mrs. Poornima

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J U D G M E N T

Dr.Vineet Kothari,J

Whether the Income Tax Law is a-political, a-religious in character, whether the character and attributes of the recipient of an income determines the taxability or the character of the receipt of income and whether the provisions for withholding of tax or deduction of tax at source are dependent upon the final taxability of the sum paid or not, are the background cords, in which, we are called upon to decide a few important questions of law arising in the present Writ Appeals filed by the Union of India and Income Tax Department, arising from the judgment of the learned Single Judge, by which he allowed the writ petitions filed by the respondent/assessees, the Christian Religious Institutions, which run and control a large number of educational institutions, Convents or Schools in the State of Tamil Nadu and who represent the cause of the Teachers working in such Schools, mainly the Nuns, Sisters, Missionaries and Fathers, who are also Teachers in such Schools of the various subjects.

2. The crux of controversy is that the Nuns, Sisters, Priests or Fathers, who also render their services as Teachers in these schools which receive Grant-in-aid from the State Government under the Grant-in-Aid Schemes formulated by the State to the extent of their full salary, claim that they are bound by the Canon Law for their vows of poverty to the Christ and that they cannot be taxed in respect of the Grant-in-Aid or salary received from the State Government by respective school or educational institutions and now directly transferred to the individual Bank Account of the Teachers under ECS Scheme, as the receipt of salary in their hands entirely belongs to the Institution, Church or the Religion and having taken such vows of poverty etc. in their Canon Law, they have suffered a civil death and renounced the world and therefore, they cannot be subjected to the deduction of tax at source as stipulated in Section 192 of the Income Tax Act, 1961, and for which, in the recent past, the Income Tax Department instructed the concerned authorities of the State Government to deduct income tax at source on the payment of salaries made to these Teachers, nuns, etc. along with other Teachers also who are employed in such Schools and consequently, the relevant Instructions of the Income Tax Department in this regard deserve to be quashed.

3. The learned single Judge, in the judgment under appeal rendered on

22.12.2016 in W.P.Nos.37565 to 37567 of 2015, etc. (Institute of the Fransican Missionaries of Mary v. Union of India and Others), allowed the said writ petitions upholding the aforesaid contention of the Assessee Institutions and the Missionaries, discussing the Canon Law in detail and held that no income tax can be deducted at source from the salaries and other monetary benefits paid to these persons, who are the Members of the Religious Congregation and it would be sufficient, if the Head of the Institution concerned certifies the names of the staff Members, who were Members of the Religious Body and the period during which they have served and the designation of the post. While doing so, the learned Single Judge held that in terms of Article 26 of the Constitution of India, there is a guarantee to religious denomination, a right to acquire its own property and to administer such property in accordance with law and that the administration of the property by a religious denomination has thus been placed on a different footing from the right to manage its own affairs in matters of religion. The latter is a fundamental right which no legislature can take away, whereas the former can be taken away by law which the legislative can validly impose. The learned single Judge proceeded to hold that an action by an authority which impinged upon the right to practice a religion as guaranteed under Articles 25 and 26 of the Constitution of India has to be held to be as not sustainable.

4. Aggrieved by the said judgment, the Union of India and Income Tax Department have come up in the present set of writ appeals, which we heard finally at the admission stage itself, by consent of the parties and Mr.Karthik Ranganathan appeared for the Revenue, whereas Mr.Arvind Datar, learned senior counsel and Fr. Xavier Arulraj, learned senior counsel himself a Father under Canon Law, appeared on behalf of the assessee Institutions.

5. Besides the aforesaid order of the learned Single Judge passed at Principal seat at Chennai, another learned single Judge of this Court allowed a batch of writ petitions filed at Madurai Bench of Madras High Court on 03.3.2016 in WP (MD) Nos.21172 to 21181 of 2015 etc. batch (The Correspondent, Holy Cross Primary School, Golden Rock v. Central Board of Direct Taxes and Others). The learned single Judge at Madurai also allowed the writ petitions and held that upon individual Undertaking and Affidavit given by Priests or Nuns to the Income Tax Department, that his/her entire salary as Teacher/Non-Teaching Staff can be paid directly by the State Government to the Congregation or Diocese to which he/she belongs and filing of similar affidavit before the Government of Tamil Nadu, the Income Tax Department, on their satisfaction, to give a certificate or a letter to the Government of Tamil Nadu that they need not deduct tax at source insofar as

such Priests and Nuns are concerned because they will not be paying salary to the individual, but only in the name of Congregation or Diocese only. The learned counsel for the Revenue Mr.Ravi Kumar submitted before us that writ appeal on similar lines have also been filed by the Department at Madurai Bench also, which are pending consideration there.

6. The present controversy in hand takes us back to a necessary reference of certain old Circulars and Instructions issued by the Central Board of Revenue as well as the Commissioner of Income Tax, which were heavily relied upon by the Respondent Assessees also and we think it appropriate to quote them in extenso here.

I - Circular of the Central Board of Revenue, No.5 of 1940 dated 2nd January 1940

Circular No.5 of 1940

D.Dis. No.26(33)-I.T./39

CENTRAL BOARD OF REVENUE

*New Delhi, the **2nd January 1940**.*

Circular

*Liability to tax - **Fees** received by **Missionaries** and subsequently **made over to their Society***

Medical fees, examination fees or any other kind of

fees received by the missionaries are taxable in the hands of the missionaries themselves *even though under the terms of their employment or the rules of the Society to which they belong the fees have to be made over to the Society. These fees are earned by the missionaries for professional or other services rendered by them and* ***the fees are paid to them and not the Missionary Societies.*** *Not only is there an element of accrual of the fees to the missionaries but there is an actual receipt by them. The fact that they are, by the terms of their contracts, required to make over the fees to the societies does not affect the liability (cf. 2 I.T.C. 286).*

Sd/-

First Secretary, Central Board of Revenue.

All Commissioners of Income-tax.
All Appellate Assistant Commissioners.
The Income-Tax Adviser to the Board.

II - Circular of Central Board of Revenue, No.1 of 1944 dated 24th January 1944

Circular No.1 of 1944

C.No.26(48)-I.T./43

CENTRAL BOARD OF REVENUE

Simla, the ***24th January 1944.***

CIRCULAR

Liability to tax - Fees received by Missionaries and subsequently made over to their Society

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Attention is invited to the instructions contained in Board's circular No.5 of 1940/D.Dis.No.26(33)-I.T./39 dated the ***2nd January, 1940*** *and D.O. D.Dis.No.26(33)-I.T./39, dated the 9th May 1940. It has been brought to the Board's notice that* ***considerable hardship is caused to Missionaries by the taxation of fees*** *received by them for services rendered, which, by the conditions of their service and the Rules of their Society, they are required to make over to the Society. In view of the* ***principle of diversion of income*** *enunciated by the Privy Council in* ***Dudhuria's case (6 I.T.C. 449) it is arguable that fees received by Missionaries*** *on behalf of a Missionary Society and which are payable to it according to their* ***contract of service are not their income****. As recognised in the Board's D.O. letter referred to above,* ***where a Missionary employee collects fees*** *in payment of bills due to the institution the amount collected* ***will be the income of the institution and not that of the employee****. It makes little difference whether the bills are prepared by the Society and sent out for collection or whether the* ***employee collects the fees in a fiduciary capacity*** *and pays the amount over to the Society. In the circumstances, the* ***Board have decided that no income-tax should be levied on fees received***

***by Missionaries for services rendered by them**, which by the **conditions of their service and the Rules of their Society**, they are required to **make over to the Society**. Such income would also be exempt in the hands of the Society concerned **if the conditions laid down in Sec. 4(3)(ia) are satisfied**.*

*2. Board's circular No.5 of 1940 (D.Dis.No.26(33)-I.T./39) dated the **2nd January 1940 is hereby cancelled**.*

Sd/-

for First Secretary, Central Board of Revenue.

All Commissioners of Income-tax.
All Appellate Assistant Commissioners.

III - Proceedings of the Director of Public Instruction, Madras, dated 18th July, 1946.

Copy of Proceedings of the Director of Public Instruction, Madras.

*Rc.No.387/D/46, dated **18th July 1946***

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*Sub: **Acquittance for salaries** paid on behalf of members belonging to the **Catholic Religious Order***

Read: Replies from the Inspecting Officers to Director's circular Procs.C.No.387/D/46, dated 10.4.46

The Director is of opinion that there is no justification

*for insisting on the members of teaching staff belong to the Catholic Religious Orders who have taken the **vow of poverty**, passing acquittances in respect of their monthly salaries from the educational institutions for what are **purely fictitious amounts**. He therefore directs that it would be sufficient **if the head of institutions concerned certifies as follows each month**:*

"Certified that the following members of the Religious body of ..... were on duty in the (Name of the Institution)..... in the month of .....19... during the period noted against each and that the salaries assigned to them for purposes of financial statements due to the Education Department are as shown against each:-

S.No. of Post	*Designation of Post*	*Name of names of incumbents*	*Periods for which served*	*Salary assigned to each*

Name of the Institution

Date: *Head of the Institution*

The undermentioned officers are requested to bring this decision to the notice of the managements for their information and guidance.

C.D.S. Chetti

for Director of Public Instruction

IV - Letter of the Commissioner of Income Tax, Madras II, dated 30.01.1969

Office of the Commissioner of Income Tax Madras II

22, Nungambakkam High Road, Madras-34

RC.No.230....11(75) dated 30.1.1969

From

The Commissioner of Income Tax

Madras-II, Madras

To

Very Rev.Mgr.B.A. Figredo

Secretary

Madras Catholic Education Council

15, Kolandai Street

Madras - 3.

Rev.Father,

Sub: Representation for ***exemption of emoluments drawn by Priests and Religious employed*** *in Education.*

Ref: Your letter dated 9-8-1967

It has been decided that in cases where the amounts received by Priests and Religious as ***salary are subject to an overriding title by their conditions****, and rules of service to be*

*passed over to the church authorities (Whose income is exempted from tax) such amounts will n**ot be liable to be taxed.***

Yours faithfully,
(Sd.) V.Krishnamoorthy
Income Tax Officer (H.Qrs.) (Tech.)
for Commissioner

V - Circular of the Central Board of Direct Taxes, dated 5th December 1977

11B, Income Tax Exemption to Missionaries
F.No.200/88/75-II(AI)
Central Board of Direct Taxes
GOVT OF INDIA
New Delhi
Dated: 5.12.1977

To
All Commissioners of Income Tax

Sir,

*Sub: Exemption from payment of Income-Tax on **Salaries of members of Religious Congregations***

*Attention is invited to Circular No.1 of 1944 C.No.26(43)-IT 43 dated **24.1.1944** in which the liability to*

tax on the fees received by Missionaries and subsequently made over to the society had been considered. Representations have been received from the members of religious congregations situated all over the country ***regarding the taxability of the fees received by them****. The question for consideration is whether the* ***fees or the other earnings of the missionaries*** *be assessed as their income, although the same is to be made over to the congregation to which they belong under the rule there of.*

The Board have examined this issue and have decided that ***since the fees received by the missionaries are to be made over to the congregation concerned there is an overriding title to the fees*** *which would entitle the missionaries to* ***exemption from payment of income tax****. Hence,* ***such fees or earnings are not taxable in their hands****.*

These instructions may be brought to the notice of all the officers working in your charge.

Yours faithfully

(Signed)

J.F.Sharma

Secretary

Central Board of Direct Taxes

Note: ***This exemption is restricted only to the individual missionary and not to the income of the missionary per se****. Taxability of such an income gets*

transferred to the institution from the individual ***provided*** *the entire income for the* ***missionary is assessed with the income of the institution and satisfies all the rules governing Income Tax exemption given to the institution u/s. 12A***.

VI - Proceedings of the Under Secreary to the Government of India dated 26th February 2016

F.No.385/10/2015-IT(B)

Government of India

Ministry of Finance

Department of Revenue

Central Board of Direct Taxes

North Block, New Delhi

26th February, 2016

To

The President

Kerala Conference of Major Superiors (KCMS)

Near Darusalm, Thaikkattukara

PO Aluva

KERALA 638 106

Subject: Writ Appeal in Kerala High Court and Writ Petition in Madras High Court against TDS in the case of cases of Members of religious congregation-Order

dated 9.3.2015 of the Hon'ble High Court of Kerala in WP(C) 35546 of 2014- regarding

Sir,

I am directed to refer to your letter dated 29.09.2015 on the above mentioned subject. It is considered that Circular No.1 dated ***24.01.1944*** *is applicable only where "*a Missionary employee collects fees in payments of bills due to the institutions*". Considering the principle of diversion of Income, the Circular prescribed that "*The amount collected will be the income of the institution and not that of the employee. It makes little difference whether the bills are prepared by the Society and sent out for collection or whether the employee collects the fees in a fiduciary capacity and pays the amount over to the Society*". It appears that the* ***circular is applicable only on the amounts received as fees*** *towards payments of bills due to the institutions and* ***does not cover salary and pension****. A copy of Circular No.1 dated 24.1.1944 is enclosed.*

2. Further, it is noted that Instruction ***No.1121 dated 05.12.1977 basically reiterates the contents of Circular No.1 of 1944****. Circular No.1 of 1944 pertained to the Income-tax Act, 1922 and since its provisions had undergone changes in the Income-tax Act, 1961, a need was felt to clarify the issue. In this subsequent* ***Instruction of 1977, although the subject***

of the Instruction mentioned the word 'Salary', the operative portion of the instruction deals only with 'fees' received by the Missionaries *as was the case with the Circular No.1 of 1944. Therefore, it is considered that the* ***1977 Instruction has only reiterated the Circular of 1944 and has not extended its scope to cover any payment other than fees*** *received in fiduciary capacity on behalf of the congregation.*

3. In view of the above, you are requested to comment as why exemption from ***TDS may not be applicable in respect of payments received by missionary teachers in their individual capacity as remuneration for services*** *rendered by them on the basis of their individual qualifications and experience* ***which do not have the character of fees*** *collected in a fiduciary capacity and, therefore, not exempt from tax as per the Board's Circular/Instruction of 1944 and 1977.*

4. The comments in this regard may please be furnished to the Board on priority basis and positively by 8th March, 2016 so that the decision can be taken by the Board and the same can be submitted to the Hon'ble Court before the next date of hearing on 17.03.2016.

Yours faithfully,

Encl: As above

Sd/-

(Sandeep Singh)

Under Secretary to the Govt. of India

Tele: 23094182

VI - Proceedings of the DS (IT - Budget), Department of Revenue, dated 7th April 2016

F.No.385/10/2015-IT(B)

Government of India

Ministry of Finance

Department of Revenue

Central Board of Direct Taxes

North Block, New Delhi

7th April, 2016

To

The President

Kerala Conference of Major Superiors (KCMS)

Near Darusalm, Thaikkattukara

PO Aluva

KERALA 638 106

Subject: Writ Appeal in Kerala High Court and Writ Petition in Madras High Court against TDS in the cases of Members of religious congregation-Order dated 9.3.2015 of the Hon'ble High Court of Kerala in WP(C) 35546 of 2014- regarding

Sir,

I am directed to refer to the captioned order of the

Kerala High Court and your letters dated 29.09.2015, 07.03.2016 and 18.03.2016 on the above mentioned subject. It is considered that ***Circular No.1 dated 24.02.1944 is applicable only where "*****a Missionary employee collects fees in payments of bills due to the Institutions*****"****. Considering the principle of diversion of Income, the Circular had prescribed that "*The amount collected will be the Income of the Institution and not that of the employee. It makes little difference whether the bills are prepared by the Society and sent out for collection or whether the employee collects the fees in a fiduciary capacity and pays the amount over to the Society*". **Thus the circular is applicable only on the amounts received as fees** towards payments of bills due to the institutions and does not cover salary and pension, which the missionaries earn in their individual capacity.*

2. Further, it is noted that Instruction No.1121 dated ***05.12.1977 basically reiterates the contents of Circular No.1 of 1944.*** *Circular No.1 of 1944 pertained to the Income-tax Act, 1922 and since its provisions had undergone changes in the Income-tax Act 1961, a need was felt to clarify the issue. In the subsequent Instruction of 1977,* ***although the subject of the instruction mentioned the word 'Salary', the operative portion of the Instruction deals only with 'fees' received by the missionaries****, as was the case with the Circular No.1 of 1944. Therefore, it is considered that the Instruction of 1977*

has only reiterated the Circular of 1944 and has not extended its scope to cover any payment other than fees received in fiduciary capacity on behalf of the congregation. ***Accordingly, salary and pension earned by the members of the congregation in lieu of services rendered by them in their individual capacity are taxable in the hands of the members themselves even if the same are made over the congregation.***

3. In view of the above, ***no exemption from TDS is envisaged under the Circulars and Instructions of the Board*** *under reference in respect of payments received by members of religious congregations in their individual capacity as remuneration for services rendered by them on the basis of their individual qualifications and experience which do not have the character of fees collected in a fiduciary capacity.*

This issues with the approval of Chairman, CBDT.

Yours faithfully,

Sd/-

SHAILESH THAKUR

DS(IT-Budget), Department of Revenue

Tel: 011-23092641

Email: dsbud-cbdt@nic.in....

Copy to: Principal CCIT, Kerala with request to apprise the Hon'ble High Court of the Board's considered opinion as outlined in the letter above.

7. The learned counsel for the Revenue, Mr.Karthik Ranganathan, has raised the following contentions on behalf of the Appellant Revenue before us.

8. Mr.Karthik Ranganathan submitted that Section 192 of the Income Tax Act, 1961, mandates that any person responsible for paying any income chargeable under the head "Salaries" shall, at the time of payment, deduct income tax on the amount payable at the average rate of income tax computed on the basis of rates in force for the financial year in which the payment is made on the estimated income of the Assessee under this head for that financial year.

9. The learned counsel for the Revenue submitted that the State Government is responsible for paying the salary to the Teachers in these recognised and approved educational institutions in the form of Grant-in-Aid, irrespective of the fact whether such Teacher is a Sister or Nun or Missionary or any other person who is not affiliated with Canon Law, Church or Diocese in any manner, but is still employed as a Teacher in these educational institutions run and managed by such religious institution and therefore, irrespective of caste, sex or Religious Order to which such person is bound by or has surrendered to, the State Government is responsible and under an

obligation to deduct income tax at source on such payments which are undoubtedly taxable under the Head of "Salaries" at the time of payment thereof. He submitted that failure to deduct tax at source can render the persons obliged to do so, liable for penalty and prosecution, under the Act.

10. The learned counsel urged that the said provision of Section 192 of the Act does not recognise any aspect of religious character of the person receiving such salary and therefore, irrespective of the Religious Order to which a recipient Teacher may belong or any person receiving the salary, the payer of the amount, namely the State Government, is bound to deduct the income tax at source.

11. The learned counsel for the Revenue vehemently submitted that if the Nuns, Sisters or Missionaries who have taken the vows as per Canon law and have surrendered themselves to the Religion of Christianity, have to make over the amount of salary received by them to the Institution itself, that may just be a case of an application of their income, for whatever purpose they are obliged to so surrender as per their vows taken, but that has nothing to do with the taxability aspect of such salary received by them, much less having any prohibitive effect on the requirement of deducting taxes at source under Section 192 of the Act and the payer of such salary,

namely the State Government, is obliged to deposit such amount of tax deducted at source with the Treasury in the account of Income Tax Department, and of course the credit of such TDS can be taken by the recipient of such income against his tax liability, including the said receipt of salary from the State Government, depending upon the final tax liability of the person concerned. The tax deducted at source made under Section 192 of the Act is nothing but an advance tax on behalf of the Assessee, namely the recipient of the salary, with the Income Tax Department subject to adjustment upon the final assessment of tax liability in the hands of the recipient.

12. The learned counsel submitted that though no such assessment proceedings had been undertaken against the Teachers belonging to said class of Nuns, Missionaries etc. so far, but the Income Tax Department authorities are free and reserve their right to do so and the obligation of filing returns and subjecting themselves to assessment as provided in the Income Tax Act, is applicable to this class of Teachers of the Assessees also.

13. Mr.Karthik Ranganathan also questioned the locus standi of the educational institutions themselves instead of affected Teachers themselves to file such writ petitions challenging the action of tax deduction at source

from the salary payments made in the form of Grant-in-Aid by the State Government. He submitted that the salary was being paid to the individual teachers under the ECS (Electronic Clearance Service) method now, after 2015 and prior to this, a lumpsum amount of Grant-in-Aid on account of the salary payable to all the Teachers was made over to the Institution concerned, which distributed the said amount of salary to various teachers including the Missionaries or Nuns, etc. and they were also liable to deduct tax at source as persons responsible for paying the salary and therefore, the receipt of salary in the hands of teachers concerned, irrespective of their class or belonging to any Religious Order or not, was taxable in their hands and as such, no exemption under Section 10 of the Act was available in respect of such salary income to the Teachers.

14. The learned counsel for the Revenue also submitted that the exemption under Section 11 available to the charitable and religious Trusts would be available to the respective religious institutions, subject to the conditions stipulated in those provisions, but that does not have any bearing on the taxable character of the salary income paid by the State to these Teachers, including Nuns and Missionaries and therefore, there is no question of treating the salary income as exempt in the hands of the Teachers. Therefore, the Institutions could not agitate against the tax deduction at

source on the payment of salary to these Teachers.

15. The learned for the Revenue also submitted that the old Circulars of 1940 and 1944 as also that of 1977 quoted above and relied upon by the Assessee Institutions on the side opposite, applied only to '**fees**' received by Missionaries and were not applicable to the receipt of salary paid by the State Government involved in the present case. He submitted that the said old circulars, some issued prior to Independence and much before the 1961 Income Tax Act came into force, stood clarified by the later Instructions of the Central Board of Direct Taxes vide Instructions dated 26th February 2016 and 7th April 2016, which are also quoted above, wherein it was clearly clarified by the Central Board of Direct Taxes that any payment other than fees received in fiduciary capacity on behalf of Congregation was taxable in the hands of Members themselves, even if the same are made over to the Congregation or Religious Order and no exemption from income tax deducted at source provision, is envisaged under those old Circulars. In other words, tax deducted at source is required to be made on payment of such salary to the Teachers. These clarifications, he urged, were issued in view of similar controversy decided by Kerala High Court in favour of the Assessees against which the Department has filed Writ Appeals in Kerala High Court also and the same are also pending before Division Bench of the Kerala High Court.

16. Mr.Karthick Ranganathan, learned Standing Counsel, also raised a contention with reference to Sections 60 and 62 of the Act in Chapter V of the Act, which provides for income of other persons to be included in Assessee's total income or popularly known as clubbing provisions and he submitted that Section 60 provides that all income arising to any person by virtue of a transfer whether revocable or not, where there is no transfer of the assets from which the income arises, the said income will continue to be chargeable in the hands of the transferor. In other words, he submitted that where the contract of employment as Teacher is not transfer to the Institution, the income arising from such contract will continue to be taxed in the hands of the Transferor, namely the teacher.

17. With reference to Section 62 of the Act, which envisages a transfer revocable after a specified period only, learned counsel submitted that even if the Nuns or Missionaries are deemed to have surrendered to the Institution or Religion, but if they can come out of that Order on their own volition, in such circumstances also, such income would be taxable in their hands, because they derived direct or indirect benefit from such transfer. Sub-section (2) of Section 62, he urged, that all income arising thereof by virtue of any such transfer shall be chargeable to income tax as the income of the

transferor as and when the power to revoke the transfer arises and then shall be included in his total income.

18. We may observe here itself that we are not much impressed with this argument of the learned counsel for the Revenue as the concept of transfer of an Asset or irrevocable transfer for a specific period as envisaged in Sections 60 and 62 of the Act cannot be applied to the present case, as no transfer of asset as such has taken place and the claim of the Assessee is based on their surrender or civil death on account of adopting a particular Religious Order and therefore, the receipt in the form of salary not being taxable in their hands and their claim that the receipt of salary by them actually belong to the Institution which they serve, in the name of Christ and whatever are the receipts, it belongs to the Institution itself and therefore, the tax deducted at source provision will not stand attracted, and accordingly, we reject the said last argument of the learned counsel for the Revenue at the threshold itself.

19. The learned counsel for the Revenue has relied upon various case laws which would be discussed hereinafter at appropriate place.

20. On the other hand, Mr.Arvind Datar and Fr. Xavier Arulraj, learned

senior counsel, opposed all the aforesaid submissions of the learned counsel for the Revenue and raised the following points for our consideration.

21. Mr.Arvind Datar, learned senior counsel, urged that Nuns or Missionaries who adopted a particular Religious Order and have taken vow of poverty in their complete surrender to the Religious Order cannot be said to have entered into any service to earn any income for themselves and therefore, the Grant-in-Aid paid to them under the caption "Salary" is nothing but a receipt by them as a conduit to be passed on to the Religious Order, for which they are bound by the Canon Law, which is a codified law of Christianity and therefore, no character of taxable income can be attributed to such receipts in the hands of Nuns and Missionaries and therefore, TDS provisions cannot be applied to them.

22. The learned senior counsel for the Assessees heavily relied upon the Circulars and Instructions of 1944 and 1977 quoted above and urged that the Government being fully conscious of the surrender of the Missionaries to the Religious Order, issued the aforesaid Circulars specifically exempting the tax in the hands of such Missionaries on the fees received by them on behalf of Society in their fiduciary capacity and the same principles would apply even to the 'Salaries' paid to these Teachers under the Grant-in-Aid Schemes

of the State Government.

23. Mr.Arvind Datar, learned senior counsel, emphasised that 1977 Circular specifically addressed to all the Commissioners of Income Tax with regard to the exemption from payment of Income Tax on salaries of Members of religious Congregations after 1961 Act came into being and CBDT, held that the Board has examined this issue and have decided that since the fees received by the Missionaries are to be made over to the Congregation concerned, there is an overriding title which would exempt the Missionaries from payment of Income Tax and hence, such fees/earnings are not taxable in the hands of the Assessee.

24. Mr.Arvind Datar, learned senior counsel, therefore, emphasised that if consistently for the last 40 years the Income Tax Department as well as Central Board of Direct Taxes has taken a stand and have not imposed any income tax, therefore, without there being any change of facts or law with regard to the same, the Income Tax Department is unnecessarily invoking and applying these provisions to the salary payments now made to Nuns and Missionaries, merely because the mode of payment has been changed from the earlier lumpsum payment of Grant-in-Aid to these Institutions directly to the individual bank accounts of the Teachers under the

ECS payment system now. He also drew our attention to some of the account numbers of the Missionaries to indicate that even for them, the payment has directly gone to the common Bank Account of the educational Institution.

25. Mr.Arvind Datar, learned senior counsel urged that the receipt in the hands of these Teachers was for and on behalf of the Institutions, which are Religious Institutions in character and obviously are, therefore, exempt from any income tax and therefore, there was no justification or necessity of applying TDS on such payments made to them entailing further requirement of filing returns and claim the refunds of such advance TDS collected from payment of salaries made to them. He submitted that since these persons are not subjected to income tax at all in respect of their salary income or fees as per aforesaid CBDT Circulars of 1944 and 1977, therefore they cannot be called upon to meet all these return and assessment obligations under the Income Tax Act. There is certainly a diversion of the receipts by overriding title in favour of Religious Institutions to which they have surrendered and have taken vows of poverty etc. and consequently the later so-called clarifications issued by the Department in 2016 are of no consequence and they deserve to be quashed.

26. Relying upon the case laws which will be discussed hereinafter, Mr.Arvind Datar, learned senior counsel, concluded that the learned single Judge has therefore rightly allowed the writ petitions of the Institutions and the writ appeals filed by the Union of India deserve to be dismissed by this Court.

27. We have heard the learned counsel at length and given our earnest consideration to the rival submissions and case laws cited at the bar.

28. With great respects, we are unable to persuade ourselves to agree with the contentions placed by learned senior counsel Mr.Arvind Datar and the reasons given by the learned Single Judge in the order under appeal and we are inclined to allow the present writ appeals of the Union of India and Income Tax Department for the following reasons.

29. In our opinion, the provisions relating to tax deduction at Source in Section 192 of the Act in Chapter XVII of the Act, providing for Collection and Recovery of tax in 7 Parts, wherein Part B provides for obligation on the Payer to deduct the tax at source, beginning with Section 192 relating to Salary and Section 192A series up to 194LBB and thereafter, provisions for deposit of such TDS with the Treasury and credit to be given to the Assessee

on whose behalf tax deducted at source are provided in the Act: these provisions, particularly Section 192 of the Act, which is quoted below to its relevant extent, has nothing to do with the Religious character of the Teachers who are paid such salary by the State in the form of Grant-in-aid. Whether they are Nuns, Sisters or Missionaries on the one hand or normal persons serving as Teachers in the Government Aided Schools on the other hand and their religious character or bindings have no effect on the uniform operatability of Section 192 of the Act. Section 192 reads as under:

> *"**Section 192**:*
>
> *(1) **Any person responsible for paying any income chargeable under the head "Salaries"** shall, at the time of payment, **deduct income-tax** on the amount payable at the average rate of income-tax computed on the basis of the rates in force for the financial year in which the payment is made, on the estimated income of the assessee under this head for that financial year.*
>
> *..."*

30. The said provision, without regard to the caste, colour, sex or religious bent of the person who receives the salary, makes the person responsible for paying any income chargeable under the Head "Salaries" to deduct income tax at the rates prescribed, from such payment and deposit the same in the Treasury in the Account of Income Tax Revenue Department.

State Government here is the person responsible for paying the salary. The words "at the time of payment" employed in Section 192 of the Act, in the middle of the words "Salaries" and "to deduct income tax" can be read with both sides, prefixed and suffixed word. If the income paid, at the time of payment is chargeable under the Head "Salaries" at that very point of time, the person responsible for paying the same shall deduct the income tax. The later treatment in the hands of the person who receives the income, whether it is treated as taxable or not, does not have any effect on the operation of the said provisions of Section 192 at the time of payment of salary, which is undoubtedly chargeable under the Head 'Salaries' at that point of time. This is obvious because the TDS is always made much in advance before the return of income is filed and the assessment procedure is adopted under the relevant provisions of the Act. The words "on the estimated income of the assessee" in the later part of the said Provisions of Section 192 do not envisage the determination of the issue of taxability or otherwise at that point of time and that expression is only for deciding the rates in force which will depend upon the estimated income of the Assessee under the Head "Salary". Obviously, the question of taxability or non-taxability can be decided only by the tax authorities or the Courts of law in quasi-judicial or judicial proceedings and not by the concerned persons making such payments or assessees recipients concerned. They can only make their

claims, submissions or the contention with regard to this issue. Thus, the entire claim of the Teachers, like Nuns and Missionaries in the present case, whose cause is said to be espoused by the educational institutions before us with regard to their surrender to the Religion on Canon Law, has no connection or effect on the operatability or uniform application of the said provisions of Section 192 of the Act.

31. We are further of the opinion that irrespective of their obligations by virtue of vows which they have taken, namely vows of poverty, etc. and their surrender to the Church or Diocese or civil death as they contended, the taxability of the receipt as Salary from the State Government is not effected at all. At best, it can only amount to application of their income by way of salary under that obligation towards that Religion, after they discharge their tax obligation under the Income Tax Law, out of such receipt of salary by them. Such application of salary income cannot be said to be diverted at source by overriding title and the salary as such, cannot be said to be earned by the Institution or the Religion, Church or Diocese as such. It is the individuals, be that Nuns or Missionaries or any other person who are working as Teachers, depending on their personal knowledge of subject, training and skill, for which they get the Grant-in-Aid in the form of salary from the State Government under the enactments and Schemes announced

by the State Government and therefore, the character of such receipt taxable as salary in their hands cannot be disputed and denied. The Institution, Church or Diocese does not have any legal right to directly receive that payment from the State Government, but for working of such individuals as the Teachers in those Schools.

32. The term "Salary" has been defined in Section 15 of the Act, which stipulates that any salary due from an employer or a former employer to an Assessee, including any arrears of such salary, shall be chargeable to income tax under the Head "Salary".

33. Section 15, read with Section 192, obligates the State Government or the employer, be it educational institution or the State to deduct income tax at source. Therefore, these provisions, which have no reference to the Religion, caste, colour or creed of the person concerned who receives the salary, has to be applied uniformly to all without regard to their caste, colour, creed or Religion or Religious Order by which they may bind themselves.

34. In our opinion, the provisions of Income Tax Law are dry, plain and simple, a-political, a-religious in character. In fact, except the provisions contained in Section 11 which provides for income from property held for

charitable or religious purposes to be exempt, subject to compliance of the conditions and registration by the registered Trusts etc., there is no exemption available even to the charitable or religious institutions themselves, who have to secure registration as such and then, their income and application of income for charitable or religious purposes only is regulated strictly in accordance with the provisions contained in Chapter III of the Act. These provisions have no application to the individual Nuns, Sisters or Missionaries so as to claim any exemption from income tax.

35. The same Chapter III provides for Special Provisions relating to Incomes of political parties also in Section 13A of the Act, while Section 13B of the Act provides for special provisions relating to voluntary contributions received by Electoral Trust. There is no issue raised with regard to these provisions before us in the present case and these provisions are referred just to indicate that except these special provisions with limited application, the Income Tax Law is otherwise a-political and a-religious in character.

36. As far as the provisions with which we are concerned, namely Sections 15 and 192 of the Act, we do not have an iota of doubt that these provisions have nothing to do with religion or any other special status of the person receiving the income described to be salary by the payer of the same.

37. This brings us to the next bone of contention between the parties, namely as to whether the Religious binding character of the Nuns and Missionaries to make over even their salary receipts to the Institution, Church or Diocese amounts to diversion of income at source, by overriding title in favour of the Institution, Church or Diocese towards such religious obligations or is merely an application of their salary income taxable in their hands and such application of income can obviously be made only after meeting their tax obligations under the Income Tax Act ***a priori***.

38. On the above said debatable issue of diversion of income by overriding title and application of income, we would like to refer to one of the decision dated 25th September 2018, rendered by Karnataka High Court, to which one of us was a party (Dr.Vineet Kothari,J), in the case of ***Principal Commissioner of Income Tax v. Chamundi Winery and Distillery [(2018) 97 Taxmann.com 568 = (2018) 408 ITR 402]***, In the said case, the Court discussing the legal precedents and the background of the facts that the Assessee, **Chamundi Winery**, an Excise licensee under the provisions of Karnataka Excise Act, entered into an agreement with UK based company **Diageo** and undertook the business of manufacture and sale of liquor, which was closely controlled and regulated by the State Government,

including its storage, bottling, wastage, retail and wholesale sales thereof and it was contended by Assessee Chamundi Winery that since Chamundi was only manufacturing liquor on behalf of Diageo and the receipts of sale of liquor to the Government Corporation stood diverted by overriding title to Diageo, the Assessee Chamundi was not liable to pay tax in the hands of Assessee Chamundi Winery, the Court negatived the said contention of non-taxability in the hands of Chamundi, with the following observations:

> *"The source of income as indicated above is the manufacture and sale of liquor under the Excise Licence, where **DIAGEO** has no privity or locus. Therefore, whatever income is generated out of the said business has to be first taxed in the hands of the Excise Licencee and after payment of the Income-tax, the '**distribution of surplus**' between the two parties, is their discretion and if the Assessee gets its share of total profits only to the extent of Rs.45/- per Case in the name of bottling charges and **DIAGEO** takes the entire remaining balance as per **Clauses 16 and 17** of the Agreement dated **30/10/2007**, that distribution of surplus between the two parties to the contract has no effect and overriding impact on the taxability part of the entire income arising or accruing firstly, in the hands of the Respondent Assessee **CHAMUNDI** for the period in question."*

39. A long series of case laws on the said issue of Diversion of Income

versus Application of Income was discussed by the Karnataka High Court in that decision supra, rendered on 25th September 2018 and since most of the judgments cited at bar before us in the present case have already been discussed therein, the following extract from that judgment is considered appropriate, though a lengthy one.

> *"37. In **Commissioner of Income Tax, Punjab, Himachal Pradesh and Bilaspur Vs. Thakar Das Bhargava [1960] 60 ITR 301 (SC)**, the Hon'ble Supreme Court dealing with the case of **a leading Advocate** who reluctantly accepted to appear in a Criminal trial on the condition that the monies or **Fees paid to him will be paid for a Charitable Trust** created by him. Despite the fact that the Trust was so created out of the Fees received by him, the Supreme Court held that the said **Fees was first taxable in his hands as Professional Fees** and there was **no 'diversion of income** by overriding title at source'.*
>
> *The relevant extract is quoted below for ready reference:-*
>
> > *" The assessee, an advocate, who had been originally reluctant, agreed to defend certain accused persons in a criminal trial, on condition that he would be provided with the sum of Rs.40,000 for a public charitable trust which he would create. When the trial was over the assessee was paid a sum of Rs.32,000 and he created a trust deed. The question was whether the sum of*

Rs.32,000 was the assessee's professional income:. Held, that on the facts, the proper legal inference was that the sum of Rs.32,000 paid to the assessee was his professional income at the time when it was paid to him and no trust or obligation in the nature of a trust was created at that time and when the assessee created a trust by executing the trust deed he applied part of his professional income as trust property. The desire on the part of the assessee to create a trust out of the moneys paid to him created no trust; nor did it give rise to any legally enforceable obligation. The sum of Rs.32,000 was taxable in the hands of the assessee. The rule in ***Bejoy Singh Dudhuria's case did not apply****."*

38. Further explaining the background in which the case was decided by the Appellate Authority, the Hon'ble Apex Court emphasized that ***unless the money paid was earmarked for charity ab initio*** *once such amount was received as his Professional Income, it would be so taxable in his hands.*

The relevant extract from the body of the judgment is also quoted below:-

"In the circumstances the Appellate Assistant Commissioner rightly pointed out that "if the accused persons had themselves resolved to create a charitable trust in memory of the professional aid rendered to

them by the appellant and had made the assessee trustee for the money so paid to him for that purpose, it could, perhaps, be argued that the money paid was earmarked for charity ab initio but of this there was no indication any where." In our opinion, the view taken by the Appellate Assistant Commissioner was the correct view. The money when it was received by the assessee was his professional income, though the assessee had expressed a desire earlier to create a charitable trust out of the money when received by him. Once it is held that the amount was received as his professional income, the assessee is clearly liable to pay tax thereon. In our opinion, the correct answer to the question referred to the High Court is that the amount of Rs.32,500 received by the assessee was professional income taxable in his hands."

39. In another judgment of 1960s only, the Three Judges' Bench of the Hon'ble Supreme Court in ***Provat Kumar Mitter Vs. Commissioner of Income Tax [1961] 41 ITR 624 (SC)*** *dealing with the case of the Assessee, who by a written instrument assigned the Shares of a Company in favour of his wife, held that the* ***Dividends received from such Shares would continue to be taxed in the hands of the Settlor-husband, since the Assessee merely applied his income****, since he has entered into a* ***legal obligation to apply***

it in that way, nonetheless the Dividends will remain his income*. The Privy Council decision in the case of* ***Bejoy Singh Dudhuria Vs. Commissioner of Income-tax [1933]1 ITR135 was held to be not applicable.***

The relevant extract of the said judgment is also quoted below for ready reference:-

> *"The assessee was a registered holder of 500 ordinary shares of a company. By a written instrument, dated 19-1-1953 he assigned to his wife, the right, title and interest to all dividends and sums of money which might be declared or might become due on account or in respect of those shares for the term of her natural life. However, under the terms of the instrument, the shares themselves remained the property of the assessee and it was only the income arising therefrom which was sought to be settled or assigned to his wife.*
>
> *During relevant previous year assessee's wife received dividends on those shares. In course of assessment, the ITO included dividend amount in the total income of assessee. Against the said inclusion, the assessee contended that since the settlement was for the lifetime of his wife, the third proviso to section 16(1)(c) applied and the dividend which his wife received could not be deemed to be*

his income under section 16(1)(c) and that in his case section 16(1)(c) did not apply, because there was no transfer of the shares to his wife.

... ...

... ...

In this view of the matter, it is not necessary to decide the further question if a contract of this nature operates only as a contract to be performed in future which may be specifically enforced as soon as the property comes into existence or is a contract which fastens upon the property as soon as the property comes into existence or is a contract which fastens upon the property as soon as the settler acquires it. In either view, the incomes from the shares will first accrue to the settler before the beneficiary can get it. Such income will undoubtedly be assessable in the hands of the settler despite the contract. ***We think that the true position is that if a person has alienated or assigned the source of his income so that it is no longer his, he may not be taxed upon the income arising after the assignment of the source, apart from special statutory provisions like section 16(1)c) or section 16(3) which artificially deem it to be the assignor's income.*** *But if the assessee merely applies the*

income so that it passes hrough him and goes on to an ultimate purpose, even though he may have entered into a legal obligation to apply it in that way, it remains his income. This is exactly what has happened in the present case. We need only add that the principle laid down by the Privy Council in ***Bejoy Sigh Dudhuria v. Commissioner of Income Tax [1993] 1 ITR 135 does not apply to this case****; because this is not a case of an allocation of a sum out of revenue before it becomes income in the hands of the assessee. In other words, this is not a case of diversion of income before it accrues but of application of income after it accrues."*

40. We feel this judgment applies on all fours to the case on hand, because here also, not only the Excise Licence and entire business is done in the name of the Assessee CHAMUNDI by itself, but only the income is sought to be assigned and transferred to DIAGEO which will distract the Income-Tax liability in the hands of the Assessee.

41. The Hon'ble Supreme Court in 2003 in the case of Commissioner of ***Income-Tax Vs. Sunil J. Kinariwala [2003] 259 ITR 10 (SC)*** *again* ***succinctly dealt with the earlier case laws on the issue of 'Diversion of Income by over*** *riding title at source' and in a case where the Assessee, a partner in a Firm having* ***10% share in the profits of the***

Firm, created a Trust by a Deed of Settlement assigning 50% of his 10% share of profits in favour of that Trust *of which his other relatives were the beneficiaries and the Assessee claimed that there was a diversion at source of 50% of his share of profit of 10%, the Court negatived the said plea and held that the entire 10% share in the Partnership Firm was taxable in his hands.*

42. The Hon'ble Supreme Court following the leading judgment in the case of ***Commissioner of Income-Tax Vs. Sitaldas Tirathdas [1961] 041 ITR 367 (SC)*** *held that the true test is, where by the contractual obligation, the income is diverted* ***before it reaches the Assessee****, it is deductible, but where the income is required to be only applied to discharge the contractual obligations,* ***it will not escape taxation in the hands of the Assessee so diverting his income.***

43. The relevant extract of the said judgment which in the opinion of this Court covers the case in hand before us also is quoted below for ready reference:-

> *"The assessee was a partner in a firm having a 10 per cent. share therein. He created a trust by a deed of settlement assigning 50 per cent. out of his 10 per cent. right, title and interest (excluding capital) as a partner in the firm and a sum of Rs.5,000 out of his capital in the firm in favour of the trust. The beneficiaries were the assessee's brother's wife, the*

assessee's niece and his mother. The question was whether 50 per cent. of the income attributable to his share from the firm stood transferred to the trust resulting in diversion of income at source. The Appellate Tribunal held that there was no diversion of income and that section 60 of the Income-tax Act, 1961, applied. On a reference, the High Court held that on assignment of 50 per cent. of the share of the assessee in the firm it became the income of the trust by overriding title and it could not be added to the income of the assessee. On appeal to the Supreme Court:

... ...

... ...

Held: The principle is simple enough but more often than not, as in the instant case, the question arises as to what is the criteria to determine, when does the income attributable to an assessee get diverted by overriding title? The determinative factor, in our view, is the nature and effect of the assessee's obligation in regard to the amount in question. ***When a third person becomes entitled to receive the amount under an obligation of an assessee even before he could lay a claim to***

receive it as his income, there would be a diversion of income by overriding title; but when after receipt of the income by the assessee, the same is passed on to a third person in dis-charge of the obligation of the assessee, it will be a case of application of income by the assessee and not of diversion of income by overriding title. *The decisions of the Privy Council in Raja Bejoy Singh Dudhuria v. CIT [1993] 1 ITR 135 and P.C.Mullick v. CIT [1938] 6 ITR 206 together are illustrative of the principle of diversion of income by overriding title.*

In Raja Bejoy Singh Dudhuria's case [1933] 1 ITR 135 (PC), under a com-promise decree of maintenance obtained by the step- mother of the assessee, a charge was created on the properties in his hand. The Law Lords of the Privy Council, reversing the judgment of the Calcutta High Court, held that the amount of maintenance recovered by the step-mother was not a case of application of the income of the assessee.

In contrast, in ***P.C. Mullick's case [1933] 1 ITR 135(PC),*** *under a Will, certain payments had to be made to the beneficiaries by the executors and the trustees (assessees) from the property of the*

testator. It was held by the Privy Council that such payments could only be out of the income received by the assessees and there was no diversion of income at source. Whereas in the former case, the step-mother of the assessee acquired the right to get the maintenance by virtue of the charge created by the decree of the Court on the properties of the assessee even before he could lay his hands on the income from the proper-ties, but in the latter case, the obligation of the assessee to pay amounts to the beneficiaries was required to be discharged after receipt of the income from the properties.

In CIT v. Sitaldas Tirathdas [1961] 41 ITR 367, speaking for a Bench of three learned judges of this Court, Hidayatullah J. (as he then was) having considered, among others, the aforesaid two judgments of the Privy Council laid down the test as follows (page 374):

"In our opinion, the true test is whether the amount sought to be deducted, in truth, never reached the assessee as his income. ***Obligations, no doubt, there are in every case, but it is the nature of the obligation which is the decisive fact.*** *There is a difference between an amount which a person is obliged to apply out of his income and an amount*

which by the nature of the obligation cannot be said to be a part of the income of the assessee. ***Where by the obligation income is diverted before it reaches the assessee, it is deductible****; but where the income is required to be* ***applied to discharge an obligation after such income reaches the assessee, the same consequence, in law, does not follow****. It is the first kind of payment which can truly be excused and not the second. The second payment is merely an obligation to pay another a portion of one's own income, which has been received and is since applied. The first is a case in which the income never reaches the assessee, who even if he were to collect it, does so, not as part of his income, but for and on behalf of the person to whom it is payable."*

44. In a recent decision rendered in April 2018, the Two Judges' Bench of the Hon'ble Supreme Court in the case of ***Deputy Commissioner of Income-Tax, Chennai Vs. T. Jayachandran [2018] 406 ITR 1 (SC)*** *upholding the decision of the* ***Madras High Court reported in [2013] 263 CTR 629 (Mad)*** *dealt with an interesting case of a Share Broker who was working on behalf of the Indian Bank and got only his Commission Income but was sought to be taxed for the gross receipts for the sale of Shares and Securities dealt with by him on behalf of the Indian Bank, held in favour of the*

Assessee that he was not liable to be taxed, except for his Commission Income received from the Indian Bank.

45. This judgment relied upon before us by both the Revenue and the Assessee also reiterates the aforesaid principles about the 'Diversion of Income' by an over riding title at source in the following manner:-

"(a) The Respondent - an individual and the proprietor of M/s Chandrakala and Company, is a stock broker registered with the Madras Stock Exchange. He is stated to be an approved broker of the Indian Bank. The assessment years under consideration herein are 1991-92, 1992-93 and 1993-94 respectively. During all these relevant assessment years the Respondent acted as a broker to the Indian Bank in purchase of the securities from different financial institutions.

(b) It is the case of the Revenue that the Indian Bank, in order to save itself from being charged unusually high rate of interest on borrowing money from the market, lured Public Sector Undertaking (PSUs) to make fixed term deposit with it on higher rate of interest. The rate of interest offered to the PSUs for making huge term deposits was to the extent of 12.75% of interest on fixed deposits against the

approved 8% rate of interest in accordance with the RBI directions.

(c) *In order to pay higher interest to the PSUs who made a fixed term deposit with the Indian Bank, the bank requested the Respondent to purchase securities on its behalf at a prescribed price which was unusually high but adequate to cover the market price of the securities, brokerage/incidental charges to be levied by the Respondent on these transactions, apart from covering the extra interest payable to the PSUs. The Respondent, on the instructions of Indian Bank, purchased securities at a particular rate quoted by the Bank and sold them to Indian Railways Finance Corporation. Bank of Madura was the routing bank through which the securities were purchased and sold to Indian Bank for which Bank of Madura charged service charges. The Respondent was paid commission in respect of transactions done on behalf of Indian Bank. Under instructions from Indian Bank, a portion of the amount realized from the security transactions carried on behalf of Indian Bank was paid by way of additional interest to certain Public Sector Undertakings (PSU) on the deposits made with the Indian Bank and out of eight PSUs three has*

confirmed the receipt of such additional interest through demand drafts.

(d) *The Respondent filed his return of income for the Assessment Year 1991-92 on 01.11.1993 and declared his income at Rs. 4,82,83,620/-. The total income was determined at 4,85,46,120/- vide order dated 30.06.1994. However, later on, the case was taken up for scrutiny and assessment was framed under Sec 143(3) of the Income Tax Act, 1961 (in short 'the Act'). The Assessing Officer, vide order dated 25.01.1996, raised a demand for a sum of Rs. 14,73,91,000/- with regard to the sum payable to the PSUs while holding that the Respondent has not acted as a broker in the transactions carried out for the Indian Bank rather as an independent dealer and that there was no overriding title in favour of the PSU's with regard to the additional amount earned out of the securities transactions and it is a case of application of income after accrual and, hence, the said amount is liable to be assessed as the income of the Respondent.*

... ...

... ...

The relationship between the Indian Bank and the Respondent is very much clear by the

evidence led during the criminal proceedings. The Executive Director of the Bank has specifically spoken about the role of the Respondent as a broker specifically engaged by the Bank for the purchase of securities and that the Bank has included the interest money too in the consideration paid, for the purpose of taking demand drafts in favour of PSUs. Further, the evidence led by other bank officials points out that the price of securities itself were fixed by the bank authorities and as per their directions the Respondent had purchased the securities at the market price and the differential amount was directed to be used for taking demand drafts from the bank itself for paying additional interest to the PSUs. Further, the letter dated 25.03.1994 by the Bank wherein the Bank had acknowledged the receipt of Demand Drafts taken by the Respondent gives an unblurred picture about the capacity of the Respondent in holding the amount in question. Consequently, the conduct of the parties, as is recorded in the criminal proceedings showing the receipt of amount by the broker, the purpose of receipt and the demand drafts taken by the broker at the instance of the bank are sufficient to prove the fact that the

Respondent acted as a broker to the Bank and, hence, the additional interest payable to the PSUs could not be held to be his property or income.

13) *The income that has actually accrued to the Respondent is taxable.* ***What income has really occurred to be decided, not by reference to physical receipt of income, but by the receipt of income in reality.*** *Given the fact that the Respondent had acted only as a broker and could not claim any ownership on the sum of Rs. 14,73,91,000/- and that the receipt of money was only for the purpose of taking demand drafts for the payment of the differential interest payable by Indian Bank and that the Respondent had actually handed over the said money to the Bank itself, we have no hesitation in holding that the Respondent held the said amount in trust to be paid to the public sector units on behalf of the Indian Bank based on prior understanding reached with the bank at the time of sale of securities and, hence, the said sum of Rs. 14,73,91,000/- cannot be termed as the income of the Respondent."*

46. This judgment does not help the Assessee, though the Contract/Agreement dated 30/10/2007 in the present case may prima facie reflect that the Assessee CHAMUNDI was

only entitled to get only the Bottling charges of Rs.45/- per Case, ***but that is precisely what is hoodwinking of Revenue, in the face of the fact that the entire business is carried on by CHAMUNDI only and finally profit or income is applied by way of distribution of income between CHAMUNDI getting the apportionment*** *at the rate of Rs.45/- per Case of Bottles and balance amount going to DIAGEO. The entire real income is earned by CHAMUNDI only, therefore such 'application of income' in the aforesaid agreed portions can be made only after meeting the tax obligations in the hands of CHAMUNDI itself.*

47. Clause 24 of the Agreement dated 30/10/2007 itself says respective income tax obligations will be discharged by both the parties independently.

48. The Division Bench of the ***Rajasthan High Court*** *in the case of* ***Commissioner of Income Tax Vs. Jodhpur Co-operative Marketing Society [2005] 275 ITR 372 [Raj]*** *dealt with a case of Co-operative Society which under the statutory obligations was liable to transfer 25% of its net profits to the specified funds and the Assessee Society claimed that such diversion was not taxable in its hands. Even negativing this plea of the Assessee - Co-operative Society, the Court explained the concept of 'Diversion of Income by over riding title at source' after discussing several case laws,*

some of which were cited before us also, in the following manner:-

> *"The obligation to carry a part of net profit to a reserve fund does not envisage diversion of any part of profits in person other than society itself. There is no overriding title vesting in a third party other than the assessee to lay claim to the reserve fund independent of co-operative society. The reserve fund remains part of the assessee-society's corpus and is to be applied for assessee's business only, albeit its application is being regulated by the Registrar under the provisions of the Act but the statue does not give any power even to the Registrar to utlise the reserve fund so created out of the profits of the society for any purpose other than for the purpose of the society. Even on dissolution of the society the first obligation of the assets of the society including the reserve fund as part of the total assets and not specifically, is to the discharge of its debts outstanding and obligation towards the shareholders to pay their contribution with interest and dividend payable to them for the period such dividends are not paid. Surplus, if any, left thereafter, is to be applied according to the resolution of the general body of the members of the*

society only. ***Therefore, there is no insignia of diversion of income through an overriding title vesting in a third party outside the corpus of the society itself*** *so as to consider it to be a case of diversion of income by overriding title to somebody other than the assessee. It is also to be noticed that the question of transferring any amount to the reserve fund arises only in the case the assessee society received its net profit, after paying off all its expenses"*

49. The Division Bench of the ***Madras High Court*** *in the case of* ***Commissioner of Income Tax Vs. Madras Race Club [2003] 126 Taxman 6 (Mad)****, dealt with a similar controversy involved before them in the following manner:-*

"The payments made are compulsory exactions, which if not complied with will result in the disqualification altogether of the person, who has subjected himself to the levy of penalty, fine or the requirement to take out a licence from participating in the assessee's racing activity. The power to collect these amounts is the power of the stewards and of the club generally to regulate racing and to ensure that it is carried on in an orderly fashion only with persons, who are considered competent and desirable, being allowed to take part, subject to their complying with the rules of racing. The amount of the penalties, licence fees and fines

collected are amounts which are received by the club as part of income, which it derives by conducting races. These amounts are not paid to the club by any of those, who become liable to the payment of licence fees, penalties or fines, by way of voluntary contribution from them to the benevolent fund. The amounts are not paid by them with the intention that it be a contribution to the charitable or benevolent fund. The race club itself is under no statutory compulsion to earmark or divert any part of its income for the benefit of the jockeys, apprentices, stable boys, etc.

The race club was under no statutory obligation to create a trust fund for their benefit*. The fact that the club has done so and had done so with the best of intentions,* ***does not on that score result in what is actually the income of the club, a part of which has been applied for benevolent purposes by having those amounts credited to the benevolent fund, becoming the income of the benevolent fund even at the inception.*** *The income which the benevolent fund receives is by way of the amounts which the race club has allowed to be credited to that fund, the amounts so allowed by the club to be so credited being the amounts which it has collected from the jockeys, trainers and others, who are required to take out licences and pay licence fees and the penalties and fines, which it has levied and collected from those who are participants in racing but who have not*

complied with the rules and had therefore become liable for a penalty or fine.

The amounts received by the club by way of licence fees, fines and penalties are amounts which reach the club as part of its income and which amounts after they reach the club are applied by the club for benevolent purposes by allowing the benevolent fund to have the benefit of all those amounts. The licence fees, penalties and fines at the time the payments were made by those, who are required to make those payments were, at the time the payments, not regarded by them as amounts, which were earmarked for charity and they did not regard those amounts as having been paid as contributions for a benevolent or charitable purpose. The levy as also the payment was by reason of the regulatory power vested in the assessee-club to regulate racing in accordance with the rules framed by it, non-compliance with which would result in the jockeys, trainers and others being excluded from participating in racing. The levy had direct nexus with their activity as participants in racing and the levies were designed to ensure compliance with the requirement of the rules. There was no earmarking of those amounts for the benevolent fund ab initio. The amounts collected by the club as licence fees, fines and penalties were therefore, amounts which form part of its income.

The execution of a trust deed and the inclusion of a provision in the rules of racing for crediting the sums to the benevolent fund was merely the application of a part of the income of the assessee for benevolent purpose. Creation of the benevolent fund by the trust deed and the provision made for the benevolent fund in the rules did not result in the amounts which the club was to credit to that fund being diverted at source by the overriding title of the benevolent fund to those sums. The concept of diversion of income by overriding title is to be applied in situations which are clear and where the existence of the title in the legal or natural person in whom an overriding title is to be recognized is also certain, and the facts are such as to warrant the conclusion that the income is not that of the recipient, but in fact the income of the person in whose favour an overriding title is to be recognized. A rule framed by an assessee for its own internal management cannot be elevated to the level of statutory rule and the decision on the part of the club to apply a portion of what it receives for benevolent purposes cannot be regarded as an instance of diversion by overriding title when the amounts received by the club and allowed by it to be used by the fund were not amounts, which had been paid voluntarily with the object of making those payments for charitable purposes. Diversion of the income took place after, and not before the income had reached the assessee. - CIT vs.

Bangalore Turf Club Benevolent Fund (1984) 38 CTR (Kar) 235: (1984) 145 ITR 323 (Kar): TC 44R. 1060 distinguished"

....

57. The other case law which requires a mention here from the side of the Respondent Assessee is one in the case of ***Poona Electric Supply Co.Ltd. Vs. Commissioner of Income-Tax [1965]56 ITR 521(SC)*** *in which case, the Assessee, an Electric Supply Company under the statutory Regulations made provisions for distributing or setting apart for distribution to the consumers, a part of excess over clear profits to be refunded to the consumers by way of rebate, the Court held that the* ***amounts credited by the Electricity Supply Company to the "Consumers' Benefit Reserve Account" being a part of the excess amount paid to it and reserved to be returned to the consumers, did not form part of the 'real profits' of the Company and they were diverted at source by over riding title****.*

The relevant extracts from the said judgment are quoted below for ready reference:

> *"The appellant-company is a commercial undertaking. It does business of the supply of electricity subject to the provisions of the Act. As a business concern its real profit has to be ascertained on the principles of commercial accountancy. As a licensee governed by the statute its clear profit is*

ascertained in terms of the statute and the schedule annexed thereto. The two profits are for different purposes - one is for commercial and tax purposes and other is for statutory purposes in order to maintain a reasonable level of rates. For the purposes of the Act, during the accounting years the assessee credited the said amounts to the "Consumers' Benefit Reserve Account". They were a part of the excess amount paid to it and reserved to be returned to the consumers. They did not form part of the assessee's real profits. So, to arrive at the taxable income of the assessee from the business under section 10(I) of the Act, the said amounts have to be deducted from its total income.

Income-tax is a tax on the real income, *i.e., the profits arrived at on commercial principles subject to the provisions of the Income-tax Act. The real profit can be ascertained only by making the permissible deductions.* ***There is a clear- cut distinction between deductions made for ascertaining the profits and distributions made out of profits.*** *In a given case whether the outgoings fall in one or the other of the heads is a question of fact to be found on the relevant circumstances, having regard to business principles. Another distinction that*

shall be borne in mind is that between the real and the statutory profits, i.e., between the commercial profits and statutory profits. The latter are statutorily fixed for a specified purpose. If we bear in mind these two principles there will be no difficulty in answering the question raised."

58. Similarly in another case of Electricity Supply Company only, in the case of ***Godhra Electricity Co. Ltd. Vs. Commissioner of Income-Tax 225 ITR 746 (SC)****, the Hon'ble Supreme Court held that the enhanced rate of the Electricity Supplies, which amount could not be realized by the Assessee due to litigation and subsequent take-over of the Undertaking by the Government, such amount due on account of the enhancement of rates had not really accrued to the Assessee Company and therefore, was not taxable in the hands of the Assessee Company. More so touching the concept of taxability of the "real income" rather than the "diversion of income", the Court thus held in favour of the Assessee in the said case.*

59. Both the aforesaid cases really have no application to the facts of the present case. There is no doubt that only "real income" can be brought to tax under the Act but as we have said above, what is "real income" itself is a mixed question of fact and law and therefore, it will depend upon

the facts and circumstances of each case and the law of precedents cannot be blindly applied to all the facts alike.

60. On the issue of "diversion of income at source", the learned counsel for the Assessee also relied upon a Division Bench decision of this Court in the case of ***Commissioner of Income-Tax Vs. Pompei Tile Works 175 ITR 1 (Kar)****, wherein the Division Bench of this Court held that in case of a Partnership, where the Partnership Deed provided that an outgoing Partner had to give a three months' Notice in writing of his intention to severe his/her connection with the Partnership and the continuing partners had an option to purchase his/her share at a price as provided in the Deed. On account of the disputes between the partners, one partner M was excluded from the Partnership and the new Partnership Deed provided that M should be compensated by giving 25% of the profits or if no profits were earned, 6% on the amount standing to her credit. The new Partnership Firm claimed that the amount paid to M stood "diverted at source by overriding title" and the same could not be taxed in the hands of the new Partnership Firm.*

61. Upholding the said contention, the Division Bench of this Court held as under:-

> *"Held, that on the date when the new partnership was entered into, M had pre- existing rights in the partnership and its assets. Therefore, without*

settling her rights, the other partners could not exclude her from the partnership. The partners other than M decided to exclude her and provide her compensation for the user in the new partnership of the assets of the firm to the extent of her share in the old partnership. Such a position did not result from her retirement nor severance from the partnership but from her exclusion by the other partners. Though M was not a party to the deed dated April 1, 1975, the partners of the assessee firm had to confer the benefit on M. The firm was carrying on the business of manufacture and sale of tiles; the factory was not easily divisible and the new partnership had to utilise the assets of the firm as a whole including the interest of M in the same. The business could not have been carried on without providing for such utilisation. The assessee-firm came into existence only by creating a pre-existing charge at source. The amount paid to M was diverted at source and did not form part of the assessee's income.

***CIT v. Sitalda Tirathdas [1961] 41 ITR 367 (SC) applied**."*

62. The said judgment is of little help to the Respondent Assessee in the present case before us as firstly, it is not a case of Partnership before us as the concept of mutuality and partnership has been specifically negatived and excluded in the Agreement dated 30/10/2007 between the parties before us and secondly, there is no such "diversion of profits at source" by a overriding contractual obligation. It is more of a self agreed swipe of profits from CHAMUNDI to DIAGEO, retaining only the portion of the profits in the name of the bottling charges at the rate of Rs.45/-per Case and therefore, the said judgment is of no help to the Assessee in the present case.

63. In another Division Bench decision of the Karnataka High Court relied upon by the Assessee in the case of ***Commissioner of Income-Tax Vs. Nagarbail Salt-Owners Co-operative Society Ltd. [2017] 291 CTR 287 (Kar.)****, a Co-operative Society manufacturing and selling* ***Salt on lands belonging to the land owners who were known as "Maliks"*** *and who are the Members of the Society where the activity of manufacturing and sale of Salt was undertaken by the Society and a large portion of* ***sale proceeds were transferred to an account called "Distribution Pool Fund Account" which was paid to its Members commensurate*** *with their land holdings and the remaining income was offered to tax, the Court held that logically the amount transferred to the*

"Distribution Pool Fund Account" ***cannot be taxed in the hands of the Society as income in its hands as the land in question belonged to the different Members in their own rights.***

64. ***This judgment, in our opinion, can actually be of help to the Revenue*** *rather than the Respondent Assessee when applied to the facts of the present case.Since the Excise Licence and the Liquor manufacture and sale business entirely belongs to CHAMUNDI and not DIAGEO, the income should naturally be taxed in the hands of CHAMUNDI and thereafter the "Distribution of surplus" to the extent as envisaged under the contract going to DIAGEO is nothing but only application of profits and there is no "diversion of income at source by overriding title" as was the fact before the Division Bench of this Court in the aforesaid case, viz. Nagarbail Salt-owners Co-operative Society Ltd.(supra)."*

40. Besides the discussion of aforesaid case laws, the learned counsel for the Assessee Mr.Datar also relied upon the judgment of the Supreme Court in the case of ***Commissioner of Income Tax v. Bijli Cotton Mills (P) Ltd. [(1979) 1 SCC 496]*** where the assessee company used to realise certain amounts on account of 'Dharmada', in addition to the price from its customers on sales of yarn and bales of cotton at the rate of one anna per

bundle of yarn and two annas per bale of cotton and in the bills issued to the customers, these amounts were shown in a separate column headed 'Dharmada'. The Assessee company did not credit the amounts of Dharmada so realised by it in its trading account, but maintained a separate account known as the 'Dharmada' account, to which amounts were credited and payments made out were debited from time to time. The Court in these circumstances held that such Dharmada or charity received from the customers would not form part of the price or surcharge on the price of the goods sold by the Assessee.

41. The said decision of the Supreme Court, dealing with a Trader's collection of an amount in a separate account of Dharmada (charity) with sale price of goods, with great respect, is not at all applicable to the facts involved in the case before us, dealing with receipt of salary as remuneration for the services rendered by the Teachers for the whole month and therefore, the salary income received by the Nuns or Missionaries cannot be said to have been diverted at source or inception of its accrual to them because of services as Teachers in favour of the Institution. The Institution or the Church cannot be said to have a right to receive that salary even before it reaches the Teachers, who are Nuns or Missionaries. The facts, as pointed out, that some of the receipts of salary were credited to a common bank

account of the Institution and at some places, instead of Teachers signing the receipt in the Registers maintained by the Institution only the word 'Religious' was printed there, does not alter the character of salary receipts in their hands as taxable income, much less it would prohibit the deduction of tax at source under Section 192 of the Act, by the Payer, i.e. State Government. As already stated above, it is the nature and character of receipt as salary at the time of payment which is important under the provisions of the Act.

42. Mr.Datar, learned senior counsel emphasised that the long standing practice of the Revenue Department 'not imposing any tax in the hands of the Nuns and Missionaries on such salary or Grant-in-Aid received from the State Government on the basis of the Circular issued in 1944 and 1977 does not deserve to be disturbed at this stage also', in our opinion, does not turn the tables in favour of the respondent Teachers or the educational Institutions, assuming that they have a locus standi to espouse the cause of the Teachers before this Court. It may be stated, at the outset, that the Circulars or Instructions issued by the Central Board of Direct Taxes or any authority of the Income Tax Department do not decide the question of taxability or otherwise and at best, they are only indicators of interpretation adopted by the Department and on the principles of ***contemporanea expositio***, such interpretation adopted by the Department can be held to be

only guiding the authorities subordinate to the Central Board of Direct Taxes.

43. But, the Board does not have any power to exempt a taxable income without any statutory basis available for the same. The old Circulars issued by Board referred to above and relied upon by the Assessee here on the basis of principles of Diversion of Income, which is itself an exercise of quasi-judicial adjudication being a mixed question of fact and law, could not have given a blanket exemption from tax in the hands of Nuns and Missionaries working as Teachers and earning their salary specially when these old Circulars did not refer to term 'Salary' specifically and also because the Board itself has later on held these to be not applicable to salary in 2016.

44. Consequently, we are of the opinion that an old Circular issued on 24th January 1944, much prior to Independence of the country in the year 1947 and much prior to the coming into force of the Income Tax Act, 1961 and that too vaguely worded and too narrowly worded to cover only the "fees" received by Missionaries and subsequently made over to the Society, is not taxable in their hands does not have any effect on the controversy before us. The Central Board of Revenue, as it then existed, with reference to its earlier Circular dated 9th May 1940 which was in favour of Revenue only stated in the context of medical fees, examination fees or any other kind

of fees received by the Missionaries and in view of their surrender to the Church or Religion was stated to be exempt subject to conditions laid down in Section 4(3)(ia) of the old Income Tax Act, 1922.

45. The 1977 Circular which was strongly relied upon by the learned counsel for the Assessee, though in the subject caption refers to the words "Taxes on Salaries", but in the body of the Circular, it only talks of "fees or earnings" in the hands of the Missionaries and referring to the old Circular of 24th January, 1944, again reiterates that the same would not be taxable in the hands of the Missionaries, as there is an overriding title to such fees which would entitle the Missionaries to exemption from payment of income tax. It does not, in so many words discuss the salary received by Nuns and Missionaries as Teachers to be exempt from payment of Income Tax under 1961 Act. Therefore, read in the context of medical fees or other earnings starting from 1940 Circular with 1944 Circular, this Court does not find it clear and categorical stand of the Department in the contemporary period about the exemption being available to the Missionaries with respect to salaries received by them under the Grant in Aid Schemes of the State Government, which came into force much after the independence of the country in 1947 and for the period in question before us, when such Grant-in-Aid were paid by the State Government to the Teachers directly under the

direct transfer to the bank accounts under ECS Scheme. As noted above, the said old Circulars themselves have been overridden and clarified by the subsequent Circulars of 26th February 2016 and 7th April 2016 quoted above, in which the Board has clearly stated that these old Circulars will not cover the case of Salary and Pension payable to such Nuns or Missionaries working as Teachers. The said Circulars of 2016 were issued with reference to pendency of writ petition before the Kerala High Court on the same grounds which are urged before us here. We have already stated above that Board itself does not have power to declare any taxable income as exempt from two without the clear provisions in the Act itself.

46. The learned Single Judge of the Kerala High Court in the case of ***Fr. Sabu P.Thomas v. Union of India [2015 SCC Online Ker. 766]***, dealt with the same controversy about the deduction of tax at source from the payment of salary/pension made by the Government to persons/members of the Religious Congregations. The learned Single Judge held as under:

> *"16. In the light of the principles that can be culled out from the decisions referred to above, I am of the view that for the concept of diversion of income by overriding title to apply,* ***the diversion of income must be effective at the stage when the amount in question leaves the source, on its way***

to the intended recipient. *At that stage, on account of a* ***pre-existing legal obligation, the amount should be diverted to another****, who can claim it as of right, based on the pre-existing legal arrangement.* ***The person to whom the amount is diverted should have a legal right that entitles him to claim the amount directly from the source, and without the intervention of the person who would have received the amount but for the said legal arrangement****. Viewed from that angle, the nature of the receipt would also have a bearing on the issue of whether the amount in question reached the member of the congregation or was diverted to the congregation, without reaching the member, by way of overriding title. The receipts in question, in the instant cases, are amounts* ***by way of salary and pension. These payments accrue to the individuals concerned, who have rendered service in their individual capacity*** *and based on the educational qualifications and skills possessed by them as individuals. The* ***right to receive*** *payments by way of salary or pension also,* ***consequently, accrues or arises to them as individuals and not to the congregation*** *of which they are members.* ***No doubt, the precepts of Canon Law might require them to entrust the amounts so received to the religious*** *congregation of which they form a part,* ***but in my view the said obligation of the member, which is only an obligation based on personal law, would not clothe the***

> ***religious congregation with a legal right to receive salary/pension payments directly from the Government/Employer, and without involving the member.*** *Consequently, the entrustment of the amounts received by the member, to the congregation, would tantamount only to an application of income by the member in favour of the congregation.* ***It will not be a case of diversion of income by way of overriding title****."*

47. About the Circulars and Instructions, the learned Single Judge of the Kerala High Court proceeded to hold as under:

> *" ... 7. Circulars and instructions issued by the Board are no doubt binding in law on the authorities under the respective statutes, but when the Supreme Court or the High Court declares the law on the question arising for consideration, it would not be appropriate for the court to direct that the circular should be given effect to and not the view expressed in a decision of this Court or the High Court. So far as the clarifications/circulars issued by the Central Government and of the State Government are concerned they* ***represent merely their understanding of the statutory provisions. They are not binding upon the court****. It is for the court to declare what the particular provision of statute says and it is not for the executive. Looked at from another angle,* ***a circular which is contrary to the statutory provisions has really no existence in law.****"*

19. As has already been noticed above, an analysis of the decisions of the Supreme Court on the subject indicates that, for the concept of diversion of income by overriding title to apply, the diversion of income must be effective at the stage when the amount in question leaves the source, on its way to the intended recipient. At that stage, on account of a pre-existing legal obligation, the amount should be diverted to another, who can claim it as of right, based on the pre-existing legal arrangement. The person to whom the amount is diverted should have a legal right that entitles him to claim the amount directly from the source, and without the intervention of the person who would have received the amount but for the said legal arrangement. The nature of the receipt would also have a bearing on the issue of whether the amount in question reached the member of the congregation or was diverted to the congregation, without reaching the member, by way of overriding title.

20. Thus, while there may be instances where the receipt of fees or other earnings by members of religious congregations do get diverted by overriding title to the congregation, ***the proposition is by no means an absolute one that is applicable in all cases of earnings by a member of the religious congregation****. The applicability of the concept would have to be tested on the* ***facts of each case, by examining the nature of the receipt by the assessee****. Viewed*

in that light, the impugned instructions of the Income Tax officers, in these cases, ***to deduct tax at source from payments by way of salary and pension*** *to members of the religious congregations,* ***cannot be said to be contrary to the Circulars and Instructions issued by the CBDT****. They are simply instructions issued in situations not covered by the CBDT Circular/Instructions. Further, the CBDT Circulars/Instructions cannot be treated as encompassing receipts by way of salary and pension, as that would render the said Circulars and Instructions contrary to the law declared by the Courts on the concept of diversion of income by way of overriding title.*

21. For reasons that I have already stated, I am of the view that the payments involved in the instant cases accrued to the members of the religious congregations as their income and the subsequent diversion of that income to the religious congregation concerned was only a case of application of that income. The impugned instructions of the Income Tax Officers, that direct the persons responsible for paying Salary and Pension to members of religious congregations, to deduct tax at source in accordance with Section 192 of the IT Act, cannot be said to be illegal. ***The writ petitions****, in their challenge against the said instructions, fail and are accordingly* ***dismissed****."*

48. Though an intra-court appeal against the said judgment of the learned single Judge is said to be pending before the Division Bench of the Kerala High Court, we are of the opinion that the view taken by the learned Single Judge of the Kerala High Court is perfectly justified and is in accordance with law and we respectfully agree with the said view of the learned Single Judge of the Kerala High Court.

49. On the basis of the aforesaid, we find that the salary in question was not directly received by the Congregation or Religion by overriding diversion of title, but were paid by the State to the Teachers who are Nuns or Missionaries and thereafter, it might have been applied or made over to the Church or Diocese or the Institution run by them. Merely by illustrative view of the entry shown as deposit of salary in common bank account or such Nuns or Missionaries not signing the receipt of salary in the Registers maintained by the Institution itself is not sufficient to prove such facts for all such persons belonging to the said class and the same cannot be taken as a proof of diversion of their salary income by overriding title in favour of the Institution or the Religion. The salary is paid under the contract of employment with which Educational Institution or the Church or Diocese is not even a privy to such contract of employment qua the State Government.

50. Moreover, the State Government as a Payer of salary under Income Tax Act is not bound by any Religious tenets or provisions of Canon Law. It has nothing to do with the Religious freedom as guaranteed under Articles 25 and 26 of the Constitution of India. In the present case, the State Government cannot be said to be bound to pay such salary in favour of the Church or Diocese in place of Teachers concerned who may be Nuns or Missionaries and who may even leave and come out of such Religious Order on their own volition. On the other hand, the State Authorities, if they do not deduct tax at source on such salary payments, may be held guilty of not following the provisions of Income Tax Act rendering them to pay penalty and even face prosecution. Therefore, neither the Income Tax Department nor the State Government have anything to do with the religiious character of the Institution, may be Teachers or Nuns or Missionaries and therefore, they cannot take a stand for not making the tax deduction at source in view of the Canon Law.

51. Therefore, in our opinion, with great respects, the learned Single Judge has taken an impermissible route of Canon Law to interpret the provisions of Income Tax Law and holding such Tax Law to be of secondary importance, vis-a-vis the Canon Law applicable to the individual Teachers belonging to the class of Nuns, Missionaries or Sisters. Therefore, we are of

the considered opinion that the present writ appeals filed by the Union of India deserve to be allowed and the order of the learned Single Judge under the appeal deserves to be set aside. We accordingly allow the said appeals of the appellant Union of India and set aside the order passed by the learned Single Judge. No costs.

51. Being conscious of the fact that our reversal of the order passed by the learned Single Judge may result in practical complications for the past period for the Educational Institutions as well as Teachers belonging to said class and also the State Government and Income Tax Department on the other side, we direct that this judgment shall be applied prospectively and not for the past period.

Index : Yes
Order : Speaking

(V.K.J.) (C.V.K.J.)
20.3.2019

kpl

DR.VINEET KOTHARI,J,
and
C.V.KARTHIKEYAN,J

kpl

Judgment in
W.A.Nos.391 to 402, 569 to 583,
585 to 596, 598, 599, 603 817, 819
to 827, 829, 832, 833, 837 to 844,
846, 836 & 897 to 906 of 2019.

20.3.2019.

W.A.Nos.391 to 402, 569 to 583, 585 to 596,
598, 599 603, 817, 819 to 827, 829, 832, 833,
837 to 844, 846, 836, 897 to 906 of 2019

DR.VINEET KOTHARI, J.
AND
C.V.KARTHIKEYAN, J.

Date: 20.3.2019

In the Judgment pronounced today, there are some Respondents/Assessees, who are not represented by the learned Counsels before us. Though, prima facie, we find that those Writ Appeals are also covered by the Judgement and therefore, we have disposed of those Writ Appeals also, we direct that a copy of the said Judgment along with a copy of the present order may be sent to the Respondents/Assessees, who are not represented here before this court and they are at liberty to apply to the Court by way of appropriate Miscellaneous Application, in case the facts of their cases are different in nature, by pointing out such difference of facts with reference to the aforesaid Judgment.

(V.K.,J.) (C.V.K.,J.)
20.3.2019.

ssk.

DR.VINEET KOTHARI, J.
AND
C.V.KARTHIKEYAN, J.

ssk.

W.A.Nos.391 to 402 of 2019 & batch

20.3.2019.