SUPREME COURT OF INDIA

American Hotel & Lodging Association Educational Institute

Vs.

Central Board of Direct Taxes

C.A.No. 3468 of 2008

(S. H. Kapadia and B. Sudershan Reddy JJ.)

09.05.2008

JUDGMENT

S. H. Kapadia, J.

1. Leave granted.

2. The short question which arises for consideration in this civil appeal is as to what is the scope of enquiry by the Prescribed Authority under Section 10(23C)(vi) read with the third proviso thereto inserted by *Finance Act, 1998* w.e.f. 1.4.1999. In this case, Central Board of Direct Taxes ("CBDT") being the Prescribed Authority, at the relevant time, rejected the application for approval dated 7.4.1999 vide its order dated 12.10.2004. The said order has been upheld by the impugned judgment dated 24.11.2006 delivered by Delhi High Court in Writ Petition (C) No. 17978/04, hence, this civil appeal.

3. Briefly, the facts are as follows.

4. The claim of the appellant is that it is a non-profit organization set up in USA and has been granted tax exemption as an educational institute in that country. Appellant has a branch office in India, mainly to comply with its obligations under various agreements with Government of India (Ministry of Tourism). Its branch provides a central focal point in India for Indian missions to avail of its educational courses. Its branch collects data from educational institutions/persons wishing to take the courses offered in the field of Hospitality and fees for the required course material which is thereafter remitted to USA. After collection of data and fees, the Head Office ("HO") sends course materials, examination papers etc. to the branch in India for onward transmission to the actual user. It is the case of the appellant that, it's Indian branch is the small office in which administrative work is done. Few employees attend to this work. The costs of running the branch office is met by deducting the same from the amounts remitted to the H.O.

5. Thus, the appellant is an Institution whose objects are known as "Statement of Purposes" in *US. Under the Internal Revenue Code, 1954* in the U.S. it enjoys tax exemption status as

an educational institution. It is governed by an elected Board of Trustees and it offers high quality educational and training resources to enhance the professionalism of the hospitality industry worldwide.

6. In 1993, the National Council of Hostel Management and Catering Technology, the apex Indian body overseeing hostel management and catering education under the Ministry of Tourism, signed MoU with the Educational Institute ("EI", for short) under which approval was granted to use courses, resources and expertise of the appellant in India with a view to improve the quality of hospitality education and training in India. Consequently, the appellant opened a liaison office in Mumbai in July 1994 with the approval of Reserve Bank of India ("RBI", for short). Subsequently, in February 1995 the liaison office was upgraded to a branch office with the approval of the Ministry of Finance, GoI, and the RBI.

7. According to the MoU, the appellant has to fulfill the following obligations:

> "The Institute will:
>
> (a) Provide a full and complete, world-recognised curriculum for all hospitality education programs in India ;
>
> (b) Make available for reproduction in India the texts, course materials, and software programs utilised in the Institute's Hospitality Management Diploma ;
>
> (c) Provide a comprehensive faculty development program to upgrade the professionalism and instructional ability of those teaching hospitality management courses in India;
>
> (d) Offer a comprehensive certification and registration program for individuals currently employed in the hospitality industry in India;
>
> (e) Develop an accreditation system to permit the National Council to qualify and recognise proprietary schools;
>
> (f) Develop through grant support, an entrance test to identify individuals best qualified to enter the hospitality industry ;
>
> (g) Establish an office in India to implement and co-ordinate the Institute's activities;
>
> (h) Offer the National Council the lowest possible prices for the products and services sold to or utilised by the schools under the umbrella of the Government of India;
>
> (i) utilize Indian authors whenever possible in the development of customised programs."

8. Thus, in accordance with the terms of the said MoU, the appellant is responsible, inter alia, for providing a full and complete curriculum, recognized throughout the worldwide, for all hospitality educational programmes in India, making available text books, course materials and software programmes utilized in the appellant's Hospitality Management Diploma, offering a comprehensive certification and registration programme for Indians desiring to avail of education in the hospitality field in India. Under Clause 1(h) of the MoU, appellant is required to offer to the National Council in India, which is the apex body for hospitality management in India, lowest possible prices for its products/services to be utilized for Schools under the umbrella of GoI. Under Clause 2(b) of the said MoU, the National Council of Hospitality is obliged to utilize the appellant's courses in its current and future Hospitality Management Schools.

9. At this stage, it may be noted that the appellant got exemption under Section 10(22) up to the year ending 31.3.1998. The branch office accounts during the said period showed the gross amounts collected on the income side and the costs for running the branch were shown on the expenditure side. The difference between these figures represented what was receivable by the HO from the branch for the provision of course materials and other services provided by the HO. These accounts were accepted by the Department till 31.3.1998.

10. One more fact needs to be mentioned. Appellant herein had also moved the AAR under Section 245Q(1) of the 1961 Act for a ruling from the Authority on the following questions:

> "(i) Whether the applicant would be entitled to exemption under Section 10(22) of the Income-tax Act, 1961, in respect of its various amounts of income from the following sources in India:
>
> (a) Conducting various courses and certification programmes in hospitality management and operations.
>
> (b) Providing educational and training materials.
>
> (c) Conducting seminars, workshops and other programmes.
>
> (d) Providing training, course materials and instructional resources to the in-house faculty of various institutions.
>
> (ii) Whether the applicant would be entitled to exemption under Section 11 of the *Income-tax Act, 1961*?"

11. By its decision dated 14.2.96 the Authority held, after reviewing the objects and Agreements with GoI, that the appellant was entitled to exemption from tax under Section 10(22) of the 1961 Act. It was held that the appellant was an educational institution in terms of Section 10(22) of the 1961 Act. This decision of the Authority was accepted by the Department. It was not challenged by the Department before this Court. Thus, the

Department had accepted that the appellant's income was exempt from tax under Section 10(22) of the 1961 Act inasmuch as no assessments were made and/or no demands for income-tax was raised for all years prior to the assessment year 1999-2000 (corresponding to the accounting year ending 31.3.1999).

12. Section 10(22) stood omitted by Finance Act, 1998 w.e.f. 1.4.1999. On 7.4.1999, i.e., within seven days, appellant herein made an application to CBDT (the Prescribed Authority) for initial approval in terms of the first proviso to Section 10(23C)(vi) of the 1961 Act. The appellant applied for initial approval in the prescribed standarised form under rule 2CA of the *Income-tax Rules, 1962* i.e. Form No.56D (See: page No.62 of the civil appeal paper book).

13. Over the next 5= years CBDT did not pass any order on the appellant's application. During this period certain queries were put to the appellant which were replied to by the appellant by various letters. The important point to be noted is that by the said letters appellant clarified its position regarding the type of accounts required and maintained by its branch in India under which excess of receipts over payments was not treated as income/profit/surplus as appropriate costs incurred by the HO had not been taken into account therein because the purpose for which the accounts of the branch office were required to be made was only to establish how much money was owned to the HO and not to ascertain its income or surplus. In the said correspondence it was clarified that even the AO in assessment proceedings had accepted that the excess income over and above the expenditure shown in its account, could not be taken as appellant's income. In fact, the AO had called for information regarding the HO expenses for the year ending 31.3.1999 which had not been considered in the branch office accounts.

14. During the hearing before CBDT, appellant also furnished a certificate attested by the certified public accountant that Head Office expenses for the year ending 31.3.1999 amounted to US$.2, 63,647.The appellant also pointed out to CBDT that even the assessing officer and CIT(appeals) have not deducted the aforestated sum of alleged surplus while computing the appellant's income allegedly chargeable to tax.

15. By its Order dated 12.10.2004, CBDT rejected appellant's application holding that "there is a surplus repatriated outside India and, therefore, appellant has not applied its income for the purpose of education in India".

16. The said Order dated 12.10.2004 was challenged by the appellant in the Delhi High Court vide Writ Petition No. 17978/04. By the impugned judgment dated 24.11.2006, the Delhi High Court held that the gross receipts collected by the appellant's branch office in India is "income" chargeable to tax. It further held that since the gross receipts constituted "income" chargeable to tax such "income" was required to be applied to educational purposes in India and since the appellant had failed to do so CBDT was right in rejecting the application dated 7.4.99. In this connection, the Delhi High Court placed reliance on the third proviso to Section 10(23C)(vi) as well as the decision of this Court in the case of *Oxford University Press v. Commissioner of Income-tax*[1].

17. Shri Jehangir D. Mistri, learned counsel for the appellant, submits that the object of introducing Section 10(23C)(vi) of the 1961 Act was explained by *CBDT in its Circular No.772 dated 23.12.98*[2]. According to learned counsel, the said Circular holds that the approval contemplated by Section 10(23C)(vi) is de hors the adherence to conditions set out in the proviso to the section. In this connection, learned counsel placed reliance on the second proviso and submits that the said proviso clarifies that at the stage of approval what is required to be seen by CBDT is the nature and genuineness of the activities of the appellant-Institution under consideration. According to learned counsel, the provisos of the said section sets out conditions which must be adhered to by the Institution, and compliance therewith can never be tested at the stage of approval, since they require consideration of acts and events which will take place in the future. In this connection, learned counsel urged that application of income is the requirement mentioned in the third proviso to Section 10(23C)(vi) and that requirement can only be tested after the end of the previous year when "income" is ascertained and thereafter applied. Similarly, according to learned counsel, the requirement of accumulation, if any, in that proviso can also only be examined at the end of any previous year after "income", if any, is determined and thereafter accumulated. One more example is given by the learned counsel. The requirement of investment/deposit of funds, referred to in the third proviso, can only be tested at the stage of investment which can only take place after profit/ surplus is established. Under the 13th proviso CBDT is empowered to withdraw the approval earlier granted. That proviso, according to learned counsel, also proceeds on the basis that the withdrawal will be for failure to comply with the terms of application or investment of funds or genuineness of activities and, therefore, implicit in that proviso is an alleged violation of application of surplus and/or investment which may result in a subsequent withdrawal. In short, according to learned counsel, at the stage of grant of approval the provisos dealing with items required to be monitored, as mentioned in the third proviso, are not to be considered by CBDT and in fact it would be impossible to ascertain compliance at the stage of approval. For all the above reasons, learned counsel urges that the scope of enquiry for grant of approval under Section 10(23C)(vi) is to consider only the nature, existence for non-profit purposes and genuineness of the Institute, the remaining monitoring mechanism is not required to be considered at the stage of approval.

18. On facts, learned counsel submits that the appellant fell within the main part of Section 10(23C)(vi), excluding the monitoring conditions mentioned in the provisos and, therefore, the appellant was entitled to approval. In this connection, learned counsel submits that even CBDT in its impugned order dated 12.10.2004 has not denied the appellant's claim that it is an educational institution, existing solely for educational purposes and not for profit. In this connection, learned counsel also places reliance on the decision dated 14.2.1996 given by AAR (supra) which decision was accepted by the Department and not challenged before this Court. According to learned counsel the test to be applied, in this connection, is: whether on an overall view the object is to make profit. In this connection reliance was placed on the judgment of this Court in the case of *Additional Commissioner of Income-tax, Gujarat v. Surat Art Silk Cloth Manufacturers Association*[3]. On facts, learned counsel submits even if the branch office has incidental surplus, that does not lead to the conclusion that the

appellant-Institution exists for the purposes of profit. In short, learned counsel submits that there is no material whatsoever on the basis of which it can be said that the appellant is not an educational institution. On the contrary, learned counsel states that the appellant conducts classical education by providing course materials, designing courses, conducing examinations, granting diplomas, supervising examinations and all these activities are done under the terms of the agreement entered with the Institutions of the Government of India and, therefore, it is wholly erroneous to contend that the appellant is not an educational institution. According to learned counsel, the amounts claimed to be surplus by the Department are actually not surplus if the costs of materials and other services provided by the HO are taken into account and deducted from the fees collected. In any event, according to learned counsel, surplus/deficit is not determinative of the question as to whether the appellant exists for the profit purposes.

19. According to learned counsel, the words "in India" should not be read into clause (a) of the third proviso to Section 10(23C)(vi) of the 1961 Act as done by the High Court in its impugned judgment. Learned counsel submits that the question as to whether application of income is required to be made in India or outside India, cannot be part of the decision-making process for grant of approval. The said requirement cannot be taken into account at the approval stage. In the alternative, it is urged that in any event the said requirement of application of income in India is not there in clause (a) of the third proviso. According to learned counsel, the plain words of the third proviso refer to the application of income to the objects for which the institute is established and the said proviso does not require application of income "in India". Therefore, it is urged that there is no valid reason given by the Department as to why the words "in India" should be read in the third proviso. Ultimately, according to learned counsel, the only test required to be applied must focus on the nature, activities and genuineness of the institution and not whether such institution applies its income in India. According to learned counsel, the Indian public obtains a benefit by having internationally recognized education/qualifications available to it at the lowest possible costs. That, the benefit to the Indian public is not obtained by where the surplus is spent and therefore such criterion has no relevance to the object sought to be achieved while granting the exemption. Lastly, on this aspect learned counsel urges that similar words "in India" are found in Sections 10(20A), 10(22B) and 11(1)(a) of the 1961 Act but not in Section 10(23C)(vi). Therefore, by comparison, learned counsel urges that wherever such requirement was considered necessary by the Parliament the same has been incorporated and, therefore, the exclusion of the words "in India" in the third proviso to Section 10(23C)(vi) is not an oversight. For the above reasons, learned counsel submits that the words "in India" should not be read into clause (a) of the third proviso of Section 10(23C)(vi) of the 1961 Act.

20. Before concluding the submissions, advanced on behalf of the appellant, one aspect needs to be mentioned. Department has relied upon the judgment of this Court in the case of Oxford University Press (supra). According to learned counsel, the judgment of this Court in Oxford University Press has no application as in that case all the three Honourable Judges held that it was impermissible to read the words "in India" into Section 10(22) of the 1961 Act. According to learned counsel, the question of application of income did not arise in that case, particularly, when there were no provisos to Section 10(22) at the relevant time and,

therefore, the judgment of this Court in that case has no bearing whatsoever on the subject-matter of the present civil appeal.

21. Shri P.V. Shetty, learned senior counsel appearing for the Department, submits that the basic test which CBDT as prescribed authority ("the PA" for short) is required to consider at the stage of approval is whether the appellant's institute is solely an educational institution without profit motive. According to the learned counsel, if surplus is remitted to USA, appellant would not be entitled to approval under Section 10(23C) (vi). According to the learned counsel, in the present case, CBDT has examined the accounts of the appellant for three years and it detected that the entire expenses was not incurred in India. According to the learned counsel, Section 10(22) was the predecessor section of the present Section 10(23C)(vi). Earlier, according to the learned counsel, when Section 10(22) existed, the PA was only required to examine the objects of the Institute and not the application of income which concept is now brought in vide Section 10(23C)(vi) read with the second, third and eleventh provisos w.e.f. 1.4.1999. Therefore, according to the learned counsel, the PA has not only to examine at the stage of approval the nature of the Institution, its activities and its genuineness but also its accounts to ascertain whether the expenses incurred and the activities undertaken are in India. According to the learned counsel, "application of income" is the concept which is introduced for the first time by way of third proviso to Section 10(23C)(vi). It was not there earlier. The reason, according to the learned counsel, for insertion of the proviso to Section 10(23C)(vi) was that in the past when Section 10(22) stood alone several cases of misuse of funds by the funds not being deployed in India came to be detected. According to the learned counsel, in the past, prior to 1.4.1999, the PA used to examine only the purposes and objects for which the Institute stood established but after 1.4.1999, the PA is also required to examine application of income in India and to that extent the concept of genuineness originally mentioned in Section 10(22) now stands expanded to include even application of income to the objects for which the institute is formed. According to the learned counsel, prior to 1.4.1999, the Memorandum of Association constituted the bases for deciding the genuineness. That prior to 1.4.1999, application of income came within the concept of "assessment" in Section 11. However, that dichotomy, according to the learned counsel, now stands obliterated with the insertion of the three provisos abovementioned in Section 10(23C)(vi). Therefore, according to the learned counsel, after 1.4.1999, even the PA is required to examine whether the accrued income stood applied for educational activity in India. According to the learned counsel, not only the source of income but also its application has to be for education in India. In this connection, reliance was placed by the learned counsel on the judgment of this Court in the case of Oxford University Press (supra).

22. On merits, learned counsel submits that since an amount of Rs. 1, 30, 30,288.00 stood remitted by the appellant within the financial year ending 31.3.1999, the PA was right in rejecting the approval application made by the appellant. Learned counsel submits that the appellant is a worldwide organization. Learned counsel urged that in the application for approval, no details have been furnished by the appellant regarding its worldwide income, regarding its income in India and its expenses for its activities in India. According to the learned counsel, the burden of proof is on the applicant which it has failed to discharge.

According to the learned counsel, in the past, in several cases, funds have been diverted and, therefore, Parliament inserted several provisos in Section 10(23C)(vi) which are conditions to be complied with by the appellant. Learned counsel submits that the provisos have got to read with the main section. That, the third proviso requires application/utilization of income accruing to the appellant in India and by remitting the aforestated amount(s), the Institute herein has failed to comply with the said proviso. Learned counsel submits that the three provisos, referred to above, are further conditions, which every applicant has to satisfy. One such condition is application of income. Learned counsel submits that in order to get exemption under Section 10 (23C)(vi) the applicant has to show that it is solely and exclusively an educational institution established solely for educational purposes and not for profit and since, in the present case, the appellant has earned surplus of Rs. 1,30,30,288.00/1.14 crores, which has been remitted to USA, it is clear that the appellant's institution does not exist solely for educational purposes and that it is profit earning institute like any other commercial institute and, therefore, it is not entitled to the benefit of exemption under the said Section 10(23C)(vi). Learned counsel submits that the appellant has failed to place before the PA the requisite material to show that it is carrying out educational activity even in USA and that the entire income generated by it, both in India and in USA, is spent solely on educational activity and not to earn profits and, therefore, no interference is called for in the present case. Learned counsel submits that the appellant is claiming exemption under the Income Tax Act, 1961. That, under the said Act, exemption under Section 10(23C)(vi) is in the nature of a concession to an institution which solely carries on educational activity, which is not for profit and since Section 10 (23C)(vi) is an exemption provision, the burden is on the applicant to show the compliance of the various conditions in Section 10(23C)(vi). According to the learned counsel, the said provision must be read strictly if money laundering and shifting of profits out of India is to be prevented. According to the learned counsel, the burden is on the applicant to show from the statement of accounts of the previous year ending 31.3.1999 as to how it has derived the said surplus and how it has utilized that surplus for educational activity. In the present case, according to the learned counsel, be it surplus/profit/excess of income over expenditure, once an amount stood remitted from India to USA, it is clear that the appellant's institute is not existing solely for educational purposes in India and, therefore, is not entitled to approval under Section 10(23C)(vi). Learned counsel submits that in every case the area of activity needs to be examined by the PA. That, the applicant which seeks exemption under the above section needs to know, that education is the duty of the State; that every Institution which seeks exemption under Section 10(23C)(vi) should know that it is supposed to carry out the functions of the State in the field of education and since it is a socio-welfare function, the Legislature had stepped in by the Finance Act, 1998 so as to bring in CBDT which is the highest body of experts in the matter of granting approval. According to the learned counsel, this Court should not interfere unless reasons given by CBDT are extraneous. According to the learned counsel, the appellant's institute ought to have at the very outset, at the time of making an application, should have declared its world income, world expenditure, Indian income and Indian expenditure. That, it ought to have declared at the very outset whether the appellant's institution is an educational institution in USA. That, at the very outset, the appellant ought to have stated and given particulars regarding its activities abroad. Since it has failed to disclose the relevant aspects mentioned above, the applicant/appellant was not

entitled to approval. In conclusion, learned counsel submits that there is no dispute that certain huge amount of Rs. 1,30,30,288.00 has been remitted and that fact alone is conclusive circumstance to show that the appellant-institution is a commercial venture existing for profit and that it is not existing solely for educational purposes in India. Learned counsel urged that the third proviso brought in the concept of application of income vide the Finance Act, 1998 in order to bring about parity between universities and other educational institutions on one hand and public charitable trusts covered by Sections 11 and 12 under the 1961 Act. Therefore, according to the learned counsel, even at the stage of approval, the PA can take into account not only the nature, activities and genuineness of the Institute but also the manner in which the income derived in India is spent/utilized in India. Learned counsel submits that, in view of the Finance Act, 1998, the provisions of Section 11(1)(a) have got to be read into the provisions of Section 10(23C)(vi) and if so read the applicant-Institute is required to state in its application as to how it has utilized its Income in India in the year ending 31.3.1999. In this connection, learned counsel referred to Section 11(1)(a) which states that certain incomes shall not be included in the total income of the previous year of the person in receipt of such income if such income is derived from property held under trust, wholly for charitable or religious purposes, to the extent of which such income is applied to such purposes in India. Learned counsel submits that under Section 10(23C)(vi) as well as the third proviso thereto, the words "in India" are not there but to give purposive interpretation to the said section the court should read those words into section 10(23C)(vi) to stop shifting of the "Income"/Profits accruing in India from being transferred to US. According to the learned counsel, when the appellant herein expatriated a sum of Rs. 1,30,30,288.00 or Rs. 1.14 crores (approx.) after taking into account expenses incurred by the HO to USA, it is clear that the appellant's institution has failed to comply with the requirements of Section 10(23C)(vi) and, therefore, it is not entitled to approval. For the aforestated reasons, according to the learned counsel, no interference is called for in the present case.

23. For the sake of convenience, we quote hereinbelow the following provisions of Section 10(23C) of the 1961 Act, as amended w.e.f. 1.4.1999 vide *Finance Act, 1998*:

> "10. Incomes not included in total income.- In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included --
>
> (23C) any income received by any person on behalf of-
>
> (vi) Any university or other educational institution existing solely for educational purposes and not for purposes of profit, other than those mentioned in sub-clause (iiiab) or sub-clause (iiiad) and which may be approved by the prescribed authority; or
>
> Provided that the fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub- clause (iv) or sub-clause (v) or sub-clause (vi) or sub- clause (via) shall make an application in the

prescribed form and manner to the prescribed authority for the purpose of grant of the exemption, or continuance thereof, under sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via):

Provided further that the Central Government, before notifying the fund or trust or institution, or the prescribed authority, before approving any university or other educational institution or any hospital or other medical institution, under sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via), may call for such documents (including audited annual accounts) or information from the fund or trust or institution or any university or other educational institution or any hospital or other medical institution, as the case may be, as it thinks necessary in order to satisfy itself about the genuineness of the activities of the fund or trust or institution or any university or other educational institution or any hospital or other medical institution, as the case may be, and the Central Government or the prescribed authority, as the case may be, may also make such inquiries as it deems necessary in this behalf:

Provided also that the fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub- clause (iv) or sub-clause (v) or sub-clause (vi) or sub- clause (via)-

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[(a) applies its income, or accumulates it for application, wholly and exclusively to the objects for which it is established and in a case where more than twenty-five per cent of its income is accumulated on or after the 1st day of April, 2001, the period of the accumulation of the amount exceeding twenty-five per cent of its income shall in no case exceed five years; and]

(b) Does not invest or deposit its funds, other than-

(i) Any assets held by the fund, trust or institution or any university or other educational institution or any hospital or other medical institution where such assets form part of the corpus of the fund, trust or institution or any university or other educational institution or any Inserted by Finance Act 2001, w.e.f. 1.4.2002 hospital or other medical institution as on the 1st day of June, 1973;

[(ia) any asset, being equity shares of a public company, held by any university or other educational institution or any hospital or other medical institution where such assets form part of the corpus of any university or other educational institution or any hospital or other medical institution as on the 1st day of June, 1998;]

(ii) Any assets (being debentures issued by, or on behalf of, any company or corporation), acquired by the fund, trust or institution or any university or other educational institution or any hospital or other medical institution before the 1st day of March, 1983;

(iii) Any accretion to the shares, forming part of the corpus mentioned in sub-clause (i) and sub- clause (ia), by way of bonus shares allotted to the fund, trust or institution or any university or other educational institution or any hospital or other medical institution;

(iv) Voluntary contributions received and maintained in the form of jewellery, furniture or any other article as the Board may, by notification in the Official Gazette, specify, for any period during the previous year otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11:

Provided also that the exemption under sub- clause (vi) or sub-clause (via) shall not be denied in relation to any funds invested or deposited before the 1st

Inserted by Finance Act, 2001, w.e.f. 1.4.2001 day of June, 1998, otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11 if such funds do not continue to remain so invested or deposited after the 30th day of March, 2001:

Provided also that the exemption under sub- clause (iv) or sub-clause (v) or sub-clause (vi) or sub- clause (via) shall not be denied in relation to voluntary contribution, other than voluntary contribution in cash or voluntary contribution of the nature referred to in clause (b) of the third proviso to this sub-clause, subject to the condition that such voluntary contribution is not held by the trust or institution or any university or other educational institution or any hospital or other medical institution, otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11, after the expiry of one year from the end of the previous year in which such asset is acquired or the 31st day of March, 1992, whichever is later:

[Provided also that where the fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub- clause (vi) or sub-clause (via) does not apply its income during the year of receipt and accumulates it, any payment or credit out of such accumulation to any trust or institution registered under section 12AA or to any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) shall not be treated as application of income to the objects for which such fund or trust or institution or university or educational institution or hospital or other medical institution, as the case may be, is established:

Inserted by the *Finance Act, 2002*, w.e.f. 1.4.2003

Provided also that where the fund or institution referred to in sub-clause (iv) or trust or institution referred to in sub-clause (v) is notified by the Central Government 4[or is approved by the prescribed authority, as the case may be,] or any university or other educational institution referred to in sub-clause (vi) or any hospital or other

medical institution referred to in sub-clause (via), is approved by the prescribed authority and subsequently that Government or the prescribed authority is satisfied that-

(i) Such fund or institution or trust or any university or other educational institution or any hospital or other medical institution has not-

(A) Applied its income in accordance with the provisions contained in clause (a) of the third proviso; or

(B) Invested or deposited its funds in accordance with the provisions contained in clause (b) of the third proviso; or

(ii) The activities of such fund or institution or trust or any university or other educational institution or any hospital or other medical institution-

(A) Are not genuine; or

(B) Are not being carried out in accordance with all or any of the conditions subject to which it was notified or approved:

It may, at any time after giving a reasonable opportunity of showing cause against the proposed action to the concerned fund or institution or trust or any university or other educational institution or any hospital or other medical institution, rescind the notification or, by order, withdraw the approval, as the case may be, and forward a copy of the order rescinding the notification or

Inserted by the Finance Act, 2007, w.e.f. 1.6.2007 withdrawing the approval to such fund or institution or trust or any university or other educational institution or any hospital or other medical institution and to the Assessing Officer;]"

(emphasis supplied)

24. We may quote Section 10(22) of the 1961 Act, as it stood prior to 1.4.1999, which reads as follows:

"10. Income not included in total income- In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included-

(22) Any income of a university or other educational institution, existing solely for educational purposes and not for purposes of profit."

25. We also quote hereinbelow Section 11(1)(a) of the 1961 Act, which reads as follows:

"11. Income from property held for charitable or religious purposes.

(1) Subject to the provisions of sections 60 to 63, the following income shall not be included in the total income of the previous year of the person in receipt of the income-

(a) Income derived from property held under trust wholly for charitable or religious purposes to the extent to which such income is applied to such purposes in India; and, where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of fifteen per cent of the income from such property"

26. At the outset, we need to examine the scope of Section 10(22), which is the predecessor of Section 10(23C)(vi), without the provisos.

27. Actual existence of the educational institution was the pre-condition of the application for initial approval under Section 10(22). On grant of approval under Section 10(22), Sections 11 and 13 did not apply. Therefore, earlier prior to 1.4.1999 when exemption was given to the appellant, there was no assessment nor demand. Section 10(22) had an automatic effect. Once an applicant-institution came within the phrase "exists solely for educational purposes and not for profit" no other conditions like application of income were required to be complied with. The Prescribed Authority was only required to examine the nature, activities and genuineness of the Institution. The above phrase was the only requirement for initial approval. The mere existence of profit/surplus did not disqualify the institution if the sole purpose of its existence was not profit-making but educational activities as Section 10(22) by its very nature contemplated income of such institution to be exempted. Under Section 10(22) the test was restricted to the character of the recipient of income, viz, whether it had the character of educational institution in India, its character outside India was irrelevant for deciding whether its income would be exempt under Section 10(22).

28. The moot question in Section 10(22) was - whether the activities of the applicant came within the definition of "income of educational institution". Under Section 10(22) one had to closely analyse the activities of the Institute, the objects of the Institute and its source of income and its utilization. Even if one of the objects enabled the Institute to undertake commercial activity, the institute would not be entitled to approval under Section 10(22). The said section inter alia excludes the income of the educational institute from the Total Income.

29. In *ACIT v. Surat Art Silk Cloth Manufacturers Association (Supra)* it has been held by this Court that test of predominant object of the activity is to be seen whether it exists solely for education and not to earn profit. However, the purpose would not lose its character merely because some profit arises from the activity. That, it is not possible to carry on educational activity in such a way that the expenditure exactly balances the income and there is no resultant profit, for, to achieve this, would not only be difficult of practical realization but would reflect unsound principles of management. In order to ascertain whether the Institute is carried on with the object of making profit or not it is duty of the prescribed

authority to ascertain whether the balance of income is applied wholly and exclusively to the objects for which the applicant is established.

30. In deciding the character of the recipient, it is not necessary to look at the profits of each year, but to consider the nature of the activities undertaken in India. If the Indian activity has no co-relation to education, exemption has to be denied. (see judgment of this Court in Oxford University Press [supra]). Therefore, the character of the recipient of income must have character of educational institution in India to be ascertained from the nature of the activities. If after meeting expenditure, surplus remains incidentally from the activity carried on by the educational institution, it will not cease to do one exist solely for educational purposes. In other words, existence of surplus from the activity will not mean absence of educational purpose (see judgment of this Court in *Aditanar Educational Institution v. ACIT*[4]. The test is - the nature of activity. If the activity like running a printing press takes place it is not educational. But whether the income/profit has been applied for non-educational purpose has to be decided only at the end of the financial year.

31. In Oxford University Press (supra) this Court found that the applicant was a branch of Oxford Press which was part of the Oxford University but its activity in India was restricted to publishing books, journals, periodicals etc. The Tribunal held that because Oxford Press is part of the University its income was exempt under Section 10(22) as it stood at the relevant time. It is in this context that the words "existing solely for educational purposes and not for the purposes of profit" in Section 10(22), which words also find place in Section 10(23C)(vi), came for consideration. This Court held that location of the University is not relevant, what is relevant is - whether there is imparting of education in India. Therefore, the test formulated by this Court to decide the character of the recipient of income under Section 10(22) is whether there is in fact existence of an activity which is in the nature of "imparting of education in India". This is how the words "in India" have come into judgment and not by incorporation from Section 11(1)(a) of 1961 Act, as contended on behalf of the Department.

32. We shall now consider the effect of insertion of provisos to Section 10(23C)(vi) vide *Finance Act, 1998*. Section 10(23C)(vi) is analogous to Section 10(22). To that extent, the judgments of this Court as applicable to Section 10(22) would equally apply to Section 10(23C)(vi). The problem arises with the insertion of the provisos to Section 10(23C)(vi). With the insertion of the provisos to Section 10(23C)(vi) the applicant who seeks approval has not only to show that it is an institution existing solely for educational purposes [which was also the requirement under Section 10 (22)] but it has now to obtain initial approval from the PA, in terms of Section 10(23C)(vi) by making an application in the standardized form as mentioned in the first proviso to that section. That condition of obtaining approval from the PA came to be inserted because Section 10(22) was abused by some educational institutions/universities. This proviso was inserted along with other provisos because there was no monitoring mechanism to check abuse of exemption provision. With the insertion of the first proviso, the PA is required to vet the application. This vetting process is stipulated by the second proviso. It is important to note that the second proviso also indicates the powers and duties of the PA. While considering the approval application in the second proviso, the PA is empowered before giving approval to call for such documents including

annual accounts or information from the applicant to check the genuineness of the activities of the applicant institution. Earlier that power was not there with the PA. Under the third proviso, the PA has to ascertain while judging the genuineness of the activities of the applicant institution as to whether the applicant applies its income wholly and exclusively to the objects for which it is constituted/established. Under the twelfth proviso, the PA is required to examine cases where an applicant does not apply its income during the year of receipt and accumulates it but makes payment therefrom to any trust or institution registered under section 12AA or to any fund or trust or institution or university or other educational institution and to that extent the proviso states that such payment shall not be treated as application of income to the objects for which such trust or fund or educational institution is established. The idea underlying the twelfth proviso is to provide guidance to the PA as to the meaning of the words "application of income to the objects for which the institution is established". Therefore, the twelfth proviso is the matter of detail. The most relevant proviso for deciding this appeal is the thirteenth proviso. Under that proviso, the circumstances are given under which the PA is empowered to withdraw the approval earlier granted. Under that proviso, if the PA is satisfied that the trust, fund, university or other educational institution etc. has not applied its income in accordance with the third proviso or if it finds that such institution, trust or fund etc. has not invested/deposited its funds in accordance with the third proviso or that the activities of such fund or institution or trust etc. are not genuine or that its activities are not being carried out in accordance with the conditions subject to which approval is granted then the PA is empowered to withdraw the approval earlier granted after complying with the procedure mentioned therein.

33. Having analysed the provisos to Section 10(23C)(vi) one finds that there is a difference between stipulation of conditions and compliance thereof. The threshold conditions are actual existence of an educational institution and approval of the prescribed authority for which every applicant has to move an application in the standardized form in terms of the first proviso. It is only if the pre-requisite condition of actual existence of the educational institution is fulfilled that the question of compliance of requirements in the provisos would arise. We find merit in the contention advanced on behalf of the appellant that the third proviso contains monitoring conditions/requirements like application, accumulation, and deployment of income in specified assets whose compliance depends on events that have not taken place on the date of the application for initial approval.

34. To make the section with the proviso workable we are of the view that the Monitoring Conditions in the third proviso like application/utilization of income, pattern of investments to be made etc. could be stipulated as conditions by the PA subject to which approval could be granted. For example, in marginal cases like the present case, where appellant-Institute was given exemption up to financial year ending 31.3.1998 (assessment year 1998-99) and where an application is made on 7.4.1999, within seven days of the new dispensation coming into force, the PA can grant approval subject to such terms and conditions as it deems fit provided they are not in conflict with the provisions of the 1961 Act (including the abovementioned monitoring conditions). While imposing stipulations subject to which approval is granted, the PA may insist on certain percentage of accounting Income to be utilized/applied for imparting education in India. While making such stipulations, the PA has

to examine the activities in India which the applicant has undertaken in its Constitution, MoUs. and Agreement with Government of India/National Council. In this case, broadly the activities undertaken by the appellant are - conducting classical education by providing course materials, designing courses, conducting exams, granting diplomas, supervising exams, all under the terms of an Agreement entered into with Institutions of the Government of India. Similarly, the PA may grant approvals on such terms and conditions as it deems fit in case where the Institute applies for initial approval for the first time. The PA must give an opportunity to the applicant-institute to comply with the monitoring conditions which have been stipulated for the first time by the third proviso. Therefore, cases where earlier the applicant has obtained exemption(s), as in this case, need not be re-opened on the ground that the third proviso has not been complied with. However, after grant of approval, if it is brought to the notice of the PA that conditions on which approval was given are breached or that circumstances mentioned in the thirteenth proviso exists then the PA can withdraw the approval earlier given by following the procedure mentioned in that proviso. The view we have taken, namely, that the PA can stipulate conditions subject to which approval may be granted finds support from sub-clause (ii)(B) in the thirteenth proviso.

35. The next question which arises for consideration is: whether the words "in India" should be read into Section 10(23C)(vi) and/or in the third proviso thereto?

36. Section 10(23C)(vi) seeks to exempt income of institutions with laudable objects and activities such as universities, hospitals etc. As stated above, stipulation of monitoring conditions is different from compliance of those conditions. Compliance or non-compliance can only be gauged at the assessment stage.

37. In the case of Oxford University Press (supra), Oxford University had a branch in India. The only activity of that branch was to carry on the business of a commercial printing press which published and printed books and materials and sold the same commercially and made a profit. The Department contended that one should read the words "in India" along with the word "University". Accordingly, the Department contended that Section 10(22) exemption should be denied to the profits arising from the commercial printing activity of the University since Section 10(22) gave exemption only to profits/income of an Indian University. All the three Judges held that it was impermissible to read in the words "in India" into Section 10(22) of the 1961 Act. As stated above, Section 10(23C)(vi) is analogous to Section 10(22) of the 1961 Act. The majority view, however, was that the University must carry on educational activities in India in order to satisfy Section 10(22). According to the majority view, some educational activity had to be carried on in India and since Oxford University Press carried on no educational activity in India, the exemption did not apply to the University. In other words, the majority judges held that "non-profit" qualification has to be tested against Indian activities and it is in this context that remarks regarding "in India" are made in the judgment of the majority at page nos. 672 and 684.

38. Moreover, it is important to note that, even after the *Finance Act, 1998* w.e.f. 1.4.1999, the third proviso to Section 10(23C)(vi), which refers to monitoring conditions, confines the words "application of income" to the objects for which the Institution is established. The

third proviso does not use the words "in India" in the matter of application or accumulation of income though in several other sections like Sections 10(20A), 10(22B) and 11(1)(a) etc., Parliament has used the words "in India". Therefore, for this one more reason, we cannot read in the words "in India" into the third proviso. As stated, Parliament in its wisdom has stated in the third proviso that the educational institution has to apply its income wholly and exclusively to the objects for which it is established. Therefore, the plain words of the third proviso do not require application of income to be in India. Our judgment should not be understood to mean that the applicant has not to impart educational activities in India. If the applicant wants exemption under Section 10(23C)(vi) it has to impart education in India and only then it would be entitled to claim initial approval under that section. That is the reason for our saying that the "non-profit" qualification has to be tested against Indian activities. Our conclusion is that impartation of education must be in India if applicant desires exemption under Section 10 (23C)(vi) and that excess/deficit of income over expenditure will not decide whether the applicant exists for profit or not.

39. For the sake of clarity, we may reiterate that items such as application of income or accumulation of income or investment in specified assets indicated in clauses (a) and (b) in the third proviso are a part of compliance/monitoring conditions. As stated, however, there is a difference between application/utilization of income and outward remittance of income out of India. As discussed above, with the insertion of the provisos in Section 10(23C)(vi) of the 1961 Act, it is open to the PA to stipulate, while granting approval, that the approval is being given subject to utilization/application of certain percentage of income, in the accounting sense, towards impartation of education in India. Such exercise would be based on estimation. There is a difference between `accounting income' and `taxable income'. At the stage of Section 10, we are concerned with the accounting income. Therefore, it is open to the PA, if it deems fit, to stipulate that certain percentage of accounting income would be utilized for impartation of education in India. Therefore, in our view, it is always open to the PA to impose such terms and conditions as it deems fit.The interpretation we have given is based on harmonious construction of the provisos inserted in Section 10(23C)(vi) by the Finance Act, 1998. Lastly, we may reiterate that there is a difference between stipulation by the PA of such terms and conditions, as it deems fit under the provisos, and the compliance of those conditions by the appellant. The compliance of the terms and conditions stipulated by the PA would be a matter of decision at the time of assessment as availability of exemption has to be evaluated every year in order to find out whether the institution existed during the relevant year solely for educational purposes and not for profit.

40. In the light of what is stated above, we set aside order dated 12.10.2004 passed by CBDT; we remit the matter to CBDT for fresh consideration in accordance with law. We may clarify that, in this case, appellant has fulfilled the threshold pre-condition of actual existence of an educational institution under section 10(23C)(vi) and, therefore, on that count CBDT will not reject the approval application dated 7.4.1999.

41. Before concluding, we may state that in this case the appellant had applied for exemption in Form 56D on 7.4.1999 seeking initial approval of exemption under Section 10(23C)(vi) for the accounting year ending 31.3.1999 (assessment year 1999-2000). That application was

made under Rule 2CA of the Income-tax Rules, 1962. Under Rule 2CA, it is open to the PA to grant exemption up to 3 years. We are not concerned with the controversy as to whether the PA should grant initial approval for the accounting year ending 31.3.1999 or for three years. Suffice it to state that, one of the points which arises for determination in this case is whether the matter should be remitted to the Chief Commissioner/Director General or whether it should be remitted to CBDT because we are informed that today the PA is the Chief Commissioner/Director General and not the CBDT.

42. We quote hereinbelow Rule 2CA of the *Income-tax Rules, 1962*, which reads as follows:

> "2CA. (1) The prescribed authority under sub-clauses (vi) and (via) of clause (23C) of section 10 shall be the Chief Commissioner or Director General, to whom the application shall be made as provided in sub-rule (2).
>
> (1A) The prescribed authority under sub-clauses (vi) and (via) of clause (23C) of section 10 shall be the Central Board of Direct Taxes constituted under the *Central Boards of Revenue Act, 1963* (54 of 1963) for applications received prior to 3rd day of April, 2001:
>
> Provided that in case of applications received prior to 3rd day of April, 2001 where no order has been passed granting approval or rejecting the applications as on 31st day of May, 2007, the prescribed authority under sub-clauses (vi) and (via) of clause (23C) of section 10 shall be the Chief Commissioner or Director General.
>
> (2) An application for approval shall be made in Form No. 56D by any university or other educational institution or any hospital or other medical institution referred to in sub-clause (vi) or sub-clause (via) of clause (23C) of section 10.
>
> (3) The approval of the Central Board of Direct Taxes or Chief Commissioner or Director General, as the case may be, granted before the 1st day of December, 2006 shall at any one time have effect for a period not exceeding three assessment years. Explanation.- For the purposes of this rule, "Chief Commissioner or Director General" means the Chief Commissioner or Director General whom the Central Board of Direct Taxes may, authorize to act as prescribed authority, for the purposes of sub-clause (vi) or sub-clause (via) of clause (23C) of section 10, in relation to any university or other educational institution or any hospital or other medical institution."

43. In this case, the initial approval application in Form 56D was dated 7.4.1999. It was dismissed by CBDT on 12.10.2004 (after 5= years), therefore, in terms of Rule 2CA(1A) we are required to remit this matter to CBDT for fresh consideration in the light of the law discussed hereinabove.

44. Accordingly, the impugned judgment dated 24.11.2006 of the Delhi High Court in Writ Petition (C) No. 17978/04 as well the decision of CBDT F.No.197/78/99-ITA.I dated

12.10.2004 are set aside and the matter is remitted to CBDT for fresh consideration in accordance with law as discussed hereinabove.

45. Accordingly, this civil appeal is allowed with no order as to costs.

[1]*(2001) 247 ITR 658 SC*
[2]*[(1999)235ITR35(st.)]*
[3]*(1980) 121 ITR 1 SC*
[4]*(1997) 224 ITR 310)*