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Charitable Trusts – Recent SC Judgments

Lecture Meeting

The Chamber of Tax Consultants

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Overview

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- Educational Institutions – Denial of Claim for Registration u/s 10(23C)(vi) - *New Noble Educational Society vs CCIT [2022] 143 taxmann.com 276 (SC)*

- Applicability of proviso to section 2(15) to trusts having objects of advancement of general public utility – *ACIT(E) vs Ahmedabad Urban Development Authority [2022] 143 taxmann.com 278 (SC)*
  - Statutory Housing Boards/Corporations/Urban Development Bodies
  - Regulatory Bodies
  - Trade Promotion Organisations
  - Non-statutory Bodies set up by Government
  - Cricket Associations
  - Other Organisations

New Noble Educational Society

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- Issues which arise
  - the correct meaning of the term 'solely' in Section 10 (23C)(vi)
  - the proper manner in considering any gains, surpluses or profits, when such receipts accrue to an educational institution, i.e., their treatment for the purposes of assessment
  - in addition to the claim of an institution to exemption on the ground that it actually exists to impart education, in law, whether the concerned tax authorities require satisfaction of any other conditions, such as registration of charitable institutions, under local or state laws
- Education, i.e. imparting formal scholastic learning is what IT Act provides for under the head of charitable purposes u/s 2(15) – *Loka Shikshana Trust 101 ITR 234 (SC)* cited with approval
- *Indian Chamber of Commerce 101 ITR 796 (SC)* - profit-making cannot be an object at all in case of trusts set up with object of advancement of general public utility
- Predominant object test evolved for first time in *Surat Art Silk Cloth Manufacturers Association 121 ITR 1 (SC)* – case of advancement of general public utility, not educational institution covered by s.10(22)

New Noble – Existing Solely for Education

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- Summary of existing position re "existing solely for education":

  (i) The society/trust may not directly run the school imparting education. Instead, it may be instrumental in setting up schools/colleges imparting education. As long as sole object of the society/trust is to impart education, the fact that it does not do so itself, but its colleges/schools do so, does not result in rejection of its claim. (*Aditanar Educational Institution 224 ITR 310*).

  (ii) To determine whether an institution is engaging in education or not, the court has to consider its objects (*Aditanar*).

  (iii) The institution should be engaged in imparting education, if it claims to be part of an entity or university engaged in education (*Oxford University Press 247 ITR 658*). The mere fact that it was part of a university (incorporated or set up abroad) did not entitle it to claim exemption on the ground that it was imparting education in India.

  (iv) The judgment in *American Hotel & Lodging Association Educational Institute 301 ITR 86* states that to discern whether the applicant's claim for exemption can be allowed, the 'predominant object' has to be considered. The stage of examining whether and to what extent profits were generated and how they were utilised was not essential at the time of grant of approval, but rather formed part of the monitoring mechanism.

  (v) *Queen's Educational Society 372 ITR 699* approved and applied the 'predominant object' test (which extensively quoted *Surat Art* and applied it with approval). The court also held that the mere fact that substantial surpluses or profits were generated could not be a bar for rejecting the application for approval under Section 10(23C)(vi).

New Noble – Existing Solely for Education

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- While construing “existing solely for educational purposes and not for purposes of profit”, the seventh proviso “unless the business is incidental to the attainment of its objectives and separate books of account are maintained by it in respect of such business”, cannot be looked into
- The plain and grammatical meaning of the term ‘sole’ or ‘solely’ however, is ‘only’ or ‘exclusively’.
- It is clear that term ‘solely’ is not the same as ‘predominant /mainly’. The term ‘solely’ means to the exclusion of all others.
- None of the previous decisions – especially *American Hotel* or *Queens Education Society* – explored the true meaning of the expression ‘solely’.
- The applicable test enunciated in *Surat Art*, i.e., the ‘predominant object’ test was applied unquestioningly in cases relating to charitable institutions claiming to impart education.
- The obvious error in the opinion of this court which led the previous decisions in *American Hotel* and in *Queens Education Society* was that *Surat Art* was decided in the context of a society that did not claim to impart education - set up to advance objects of general public utility

New Noble – Existing Solely for Education

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- Approach and reasoning applicable to charitable organizations set up for advancement of objects of GPU entirely different from charities set up or established for object of imparting education
- The positive condition 'solely for educational purposes' and the negative injunction 'and not for purposes of profit' loom large as compulsive mandates, necessary for exemption
- A trust/university/institution imparting education should necessarily have all its objects aimed at imparting or facilitating education
- Interpretation of Section 10(23C) - the trust/educational institution *must solely exist* for the object it professes (education, or educational activity only), and *not for profit.*
- The seventh proviso carves an exception to this rule, and permits the trust/ institution to earn profits, provided the 'business' (viz. the education or educational activity - and nothing other than that) is incidental to the attainment of its objectives (i.e., the objectives of, or relating to, education)
- 'Incidental' means something connected with the activity of education

New Noble – Existing Solely for Education

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- The trust/educational institution, seeking approval or exemption, should solely be concerned with education, or education related activities. If, incidentally, while carrying on those objectives, the trust earns profits, it has to maintain separate books of account. It is only in those circumstances that ‘business’ income can be permitted - provided that the activity is education, or relating to education.

New Noble – Scope of Enquiry by PA

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- Whether the nature of enquiry by the PA is in any manner confined to discerning the object of the society/trust/institution at the stage when it seeks approval u/s 10(23C)
- In *American Hotel*, SC was of opinion that the question of application of income or profits could arise only at the stage of assessment – also, audited books of accounts would be of little or no relevance at the stage of registration or approval
- Having regard to the plain terms of the second proviso to Section 10(23C), which refers to the procedure for approval of applications including those made by trusts/institutions imparting education, one can discern no such restrictions
- The PA's hands are not tied in any manner whatsoever
- *American Hotel*'s decision appears to have overlooked the discretion vested in the PA to look into past history of accounts, and to discern whether the applicant was engaged in fact, 'solely' in education
- By stating that such accounts may not be available, it assumed that only newly set up societies, trusts, or institutions may apply for exemption – it equally applies to existing institutions, societies or trust, which may seek exemption at a later point

New Noble – Scope of Enquiry by PA

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- The PA should confine the inquiry ordinarily to the nature of the income earned and whether it is for education or education related objects of the society/trust
- If the surplus/profits are generated in the hands of the assessee in the imparting of education or related activities, disproportionate weight ought not be given to surpluses or profits, provided they are incidental. At the stage of registration or approval therefore focus is on the activity and not the proportion of income. If the income generating activity is intrinsically part of education, the PA may not on that basis alone reject the application.

New Noble – Registration under Other Laws

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- Requirement of registration of every charitable institution is not optional.
- Aside from the fact that consequences of non-registration are penal, which indicates the mandatory nature of the provisions of the A.P. Charities Act, such local laws provide the regulatory framework by which annual accounts, manner of choosing the governing body (in terms of the founding instrument: trust, society, etc.), acquisition and disposal of properties, etc. are constantly monitored.
- Charitable institutions and societies, which may be regulated by other state laws, have to comply with them just as in the case of laws regulating education (at all levels).
- Compliance with or registration under those laws, are also a relevant consideration which can legitimately weigh with the PA, while deciding applications for approval under Section 10 (23C)

New Noble – Incidental Business Activity

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- Imparting education through schools, colleges and other such institutions would be per se charity
- Incidental:
  - if an institution facilitated learning of its pupils by sourcing and providing text books, such activity would be 'incidental' to education
  - if a school or other educational institution ran its own buses and provided bus facilities to transport children, that too would be an activity incidental to education
  - similar instances such as providing summer camps for pupils' special educational courses, such as relating to computers etc., which may benefit its pupils in their pursuit of learning
  - providing hostel facilities to pupils would be an activity incidental to imparting education - If the institution provided hostel and allied facilities (such as catering etc.) only to its students, that activity would clearly be 'incidental' to the objective of imparting education
- If institutions provide their premises or infrastructure to other entities, trusts, societies etc., for the purposes of conducting workshops, seminars or even educational courses (which the concerned trust is not actually imparting) and outsiders are permitted to enrol in such seminars, workshops, courses etc., then the income derived from such activity cannot be characterised as part of education or 'incidental' to the imparting education - such income can properly fall under the other heads of income

New Noble – Conclusions

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a. The requirement of the charitable institution, society or trust etc., to 'solely' engage itself in education or educational activities, and not engage in any activity of profit, means that such institutions cannot have objects which are unrelated to education. In other words, all objects of the society, trust etc., must relate to imparting education or be in relation to educational activities.

b. Where the objective of the institution appears to be profit-oriented, such institutions would not be entitled to approval under Section 10(23C). At the same time, where surplus accrues in a given year or set of years per se, it is not a bar, provided such surplus is generated in the course of providing education or educational activities.

c. The seventh proviso to Section 10(23C), as well as Section 11(4A) refer to profits which may be 'incidentally' generated or earned by the charitable institution. In the present case, the same is applicable only to those institutions which impart education or are engaged in activities connected to education.

d. The reference to 'business' and 'profits' in the seventh proviso to Section 10(23C) and Section 11(4A) merely means that the profits of business which is 'incidental' to educational activity – as explained in the earlier part of the judgment i.e., relating to education such as sale of text books, providing school bus facilities, hostel facilities, etc.

e. The reasoning and conclusions in *American Hotel* and *Queen's Education Society* so far as they pertain to the interpretation of expression 'solely' are hereby disapproved. The judgments are accordingly overruled to that extent.

New Noble – Conclusions

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f. While considering applications for approval under Section 10(23C), the PA under the second proviso is not bound to examine only the objects of the institution. To ascertain the genuineness of the institution and the manner of its functioning, the PA is free to call for the audited accounts or other such documents for recording satisfaction where the institution genuinely seeks to achieve the objects which it professes. The observations made in *American Hotel* suggest that the PA could not call for the records and that the examination of such accounts would be at the stage of assessment. Whilst that reasoning undoubtedly applies to newly set up charities, the proviso under Section 10(23C) is not confined to newly set up trusts – it also applies to existing ones. The PA is not in any manner constrained from examining accounts and other related documents to see the pattern of income and expenditure.

g. It is held that wherever registration of trust is obligatory under state or local laws, the concerned trust/society/other institution etc. seeking approval under Section 10(23C) should also comply with provisions of such state laws. This would enable the PA to ascertain the genuineness of the trust, society etc. This reasoning is reinforced by the recent insertion of another proviso of Section 10(23C) with effect from 01.04.2021

New Noble – Conclusions

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- Since the present judgment has departed from the previous rulings regarding the meaning of the term ‘solely’, in order to avoid disruption, and to give time to institutions likely to be affected to make appropriate changes and adjustments, it would be in the larger interests of society that the present judgment operates hereafter. As a result, it is hereby directed that the law declared in the present judgment shall operate prospectively.
  - From AY 2023-24 onwards, or for assessments after the date of judgment?

New Noble – Issues

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- Applicable even to clauses (iiiab) and (iiiad) – term “solely” used
- Applicability to medical institutions – “solely for philanthropic purposes”
- How to determine whether objective appears profit-oriented? Would regular large surplus from activity make objective profit-oriented?
- If main activity itself is generating large surplus, how does one maintain separate books of account for business?
- Meaning of formal scholastic education – only classroom teaching of Govt recognized courses?

New Noble – Issues

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- Whether following activities would be considered as education
  - Running standalone hostel for all students
  - Conduct of examinations
  - Running nursery & kindergarten
  - Aiding students, by giving scholarships, prizes, loan scholarships by standalone trusts
  - Running unrecognized courses by other institutions – maritime training, executive development programmes,
  - Running courses in music, gemmology, computers, etc
  - Organising seminars, workshops, lecture meetings
  - Skill Training activities
  - Running workshop for Blind, Handicapped, etc

- Whether following activities of educational institutions would be regarded as incidental business
  - Running of nursery & kindergarten
  - Running unrecognised courses by educational institutions – certificate courses, executive development programmes
  - Letting of premises when not required for the school/college

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- The correct interpretation of the proviso to Section 2(15)
- Whether carrying on of any trade, commerce, or business, is a per se bar or disqualification for a GPU category charitable trust to claim to be such, precluding its tax-exempt status
- Legislative History from 1922 Act
- *Loka Shikshana Trust 101 ITR 234 - Ordinarily profit motive is a normal incidence of business activity and if the activity of a trust consists of carrying on of a business and there are no restrictions on its making profit, the court would be well justified in assuming in the absence of some indication to the contrary that the object of the trust involves the carrying on of an activity for profit …By the use of the expression 'profit motive' it is not intended that profit must in fact be earned. Nor does the expression cover a mere desire to make some monetary gain out of a transaction or even a series of transactions. It predicates a motive which pervades the whole series of transactions effected by the person in the course of his activity…."*

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- *Indian Chamber of Commerce 101 ITR 796 - The true test is to ask for answers to the following questions: (a) Is the object of the assessee one of general public utility? (b) Does the advancement of the object involve activities bringing in moneys? (c) If so, are such activities undertaken (i) for profit or (ii) without profit? Even if (a) and (b) are answered affirmatively, if (c)(i) is answered affirmatively, the claim for exemption collapses. The solution to the problem of an activity being one for or irrespective of profit is gathered on a footing of facts. What is the real nature of the activity? One which is ordinarily carried on by ordinary people for gain? Is there a built-in prescription in the constitution against making a profit? Has there been in practice, profit from this venture? Although, this last is a weak test. The mere fact that a service is rendered is no answer to chargeability because all income is often derived by rendering some service or other.*
- *Surat Art Silk Cloth Manufacturers Association 121 ITR 1 - It is clear on a plain natural construction of the language used by the legislature that the ten crucial words "**not** involving the carrying on of any activity for **profit**" go with "**object** of general public utility" and not with "**advancement**". It is the object of general public utility which must not involve the carrying on of any activity for profit and not its advancement or attainment. What is inhibited by these last ten words is the linking of activity for profit with the object of general public utility and not its linking with the accomplishment or carrying out of the object. It is not necessary that the accomplishment of the object or the means to carry out the object should not involve an activity for profit. That is not the mandate of the newly added words. What these words require is that the object should not involve the carrying on of any activity for profit. The emphasis is on the object of general public utility and not on its accomplishment or attainment.*

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- *There must be an activity for profit and it must be involved in carrying out the purpose of the trust or institution or to put it differently, it must be carried on in order to advance the purpose or in the course of carrying out the purpose of the trust or institution. It is then that the inhibition of the exclusionary clause would be attracted.*
- *It is not therefore enough that as a matter of fact an activity results in profit but it must be carried on with the object of earning profit. Profit-making must be the end to which the activity must be directed or in other words, the predominant object of the activity must be making a profit. Where an activity is not pervaded by profit motive but is carried on primarily for serving the charitable purpose, it would not be correct to describe it as an activity for profit.*
- *The test which has, therefore, now to be applied is whether the predominant object of the activity involved in carrying out the object of general public utility is to subserve the charitable purpose or to earn profit. Where profit making is the predominant object of the activity, the purpose, though an object of general public utility, would cease to be a charitable purpose. But where the predominant object of the activity is to carry out the charitable purpose and not to earn profit, it would not lose its character of a charitable purpose merely because some profit arises from the activity. The exclusionary clause does not require that the activity must be carried on in such a manner that it does not result in any profit. It would indeed be difficult for persons in charge of a trust or institution to so carry on the activity that the expenditure balances the income and there is no resulting profit*

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- *ACIT v Thanthi Trust 247 ITR 785 - The substituted sub-section (4A) states that the income derived from a business held under Trust wholly for charitable or religious purposes shall not be included in the total income of the previous year of the Trust or institution if "the business is incidental to the attainment of the objective of the Trust or, as the case may be, institution" and separate books of account are maintained in respect of such business. Clearly, the scope of sub-section (4A) is more beneficial to a Trust or institution than was the scope of subsection (4A) as originally enacted. In fact, it seems to us that the substituted sub-section (4A) gives Trust or institution a greater benefit than was given by section 13(1)(bb). If the object of Parliament was to give Trusts and institutions no more benefit than that given by section 13(1)(bb), the language of section 13(1)(bb) would have been employed in the substituted sub-section (4A). As it stands, all that it requires for the business income of a Trust or institution to be exempt is that the business should be incidental to the attainment of the objectives of the Trust or institution. A business whose income is utilized by the Trust or the institution for the purposes of achieving the objectives of the Trust or the institution is, surely, a business which is incidental to the attainment of the objectives of the Trust.*

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- The new provision, i.e., Section 2(15) of the IT Act, defined "charitable purpose" restrictively: to deny tax exemption to activities for profit which were carried on by a trust for the advancement of an object of general public utility. The reason for this change (discussed previously) was that the advantage of tax exemption was not intended to charitable trusts that were commercial concerns, which while ostensibly serving a public purpose, were fully paid for the benefits provided by them.
- The larger Bench in *Surat Art Silk* agreed with the previous decisions to the effect that the motivation for the activity in question (i.e., for it to be charitable) should not be deriving of profits. However, the larger Bench enunciated the principle of 'predominant object' and held that what was of importance was "whether the predominant object of the activity involved in carrying out the object of general public utility is to subserve the charitable purpose or to earn profit" and that such an entity would not lose its charitable character merely because some profit arose from the said activity.
- If the predominant object was not for profit, but advancement of general public utility, that some profits were earned, would not debar it from claiming to be an organization with a charitable purpose. However, if the predominant object was such that profit making was "enwrapped" or "intertwined" with it, the organization or trust could not be called charitable.

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- The view after *Surat Art Silk*, was that so long as the "dominant" object of a trust was charitable, and it did not essentially involve in business or commercial activity, generation of profits/ surpluses through activities, incidental to that main/dominant activity, did not undermine its charitable purpose, as long as the surpluses were used for advancement of an object of general public utility.
- Circulars are binding upon departmental authorities, if they advance a proposition within the framework of the statutory provision. However, if they are contrary to the plain words of a statute, they are not binding. Furthermore, they cannot bind the courts, which have to independently interpret the statute, in their own terms. At best, they may be considered as dept understanding on the subject and have limited persuasive value.
- Parliamentary endeavour was to alter the regime applicable to taxation of GPU category charities.
- This substantial change brought about by the amendments of 2008-2012 and 2015 is the prohibition from engaging in any kind of activity in the nature of business, commerce, or trade or any rendering any service in relation thereto, and earning income by way of cess, fee or consideration.
- The express deletion of reference to 'activity for profit' on the one hand, and enactment of an expanded list of what cannot be done by GPU charities if they are to retain their characteristic as charities, is an emphatic manner in which Parliament wished to express itself.

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- The impermissibility of any trade, or commercial activity or service, and income, from them, was intended to be conveyed through the prohibition, in the first part of definition of GPU charities. The necessary implication which arises is that income (received as fee, cess, or any other consideration) derived from 'prohibited activities' is necessarily motivated by profit.
- If fee or cess or such consideration is collected for the purpose of an activity, by a state department or entity, set up by statute, its mandate to collect such amounts cannot be treated as consideration towards trade or business. Therefore, regulatory activity, necessitating fee or cess collection in terms of enacted law, or collection of amounts in furtherance of activities such as education, regulation of profession, etc., are per se not business or commercial in nature. Likewise, statutory boards and authorities, who are under mandate to develop housing, industrial and other estates, including development of residential housing at reasonable or subsidized costs, which might entail charging higher amounts from some section of the beneficiaries, to cross-subsidize the main activity, cannot be characterized as engaging in business.
- If the fee or cess, or other consideration is to provide an essential service, in larger public interest, such as water cess or sewage cess or fee, such consideration, received by a statutory body, would not be considered "trade, commerce or business" or service in relation to those. Non-statutory bodies, on the other hand, which may mimic regulatory or development bodies - such as those which promote trade, for a section of business or industry, or are aimed at providing facilities or amenities to improve efficiencies, or platforms to a segment of business, for fee, whether charged by subscription, or specific fee, etc, may not be charitable; when they claim exemption, their cases would require further scrutiny.

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- Therefore, what Parliament intended through the amendments in question was to proscribe, involvement or engagement of GPU charities, from any form ("in the nature of") of activities that were trade, business or commerce, or engage or involve in providing services in relation to trade, business or commerce for a fee, cess or other consideration. The inclusion of the term "in the nature of" was by design, to clarify beyond doubt, that not only business, trade or commerce, but all activities in the nature of, or resembling them, were proscribed. Likewise, service in relation to such activities, i.e., services relating, or pertaining to, such proscribed activities, too were forbidden.
- The reference to fee or cess, is in the opinion of the court, only to emphasize that even a statutory consideration, for a service to business, trade or commerce, would take the activity outside the definition of a GPU charity.
- The paradigm change achieved by Section 2(15) after its amendment in 2008 and as it stands today, is that firstly a GPU charity cannot engage in any activity in the nature of trade, commerce, business or any service in relation to such activities for any consideration (including a statutory fee etc.). This is emphasized in the negative language employed by the main part of Section 2(15). Therefore, the idea of a predominant object among several other objects, is discarded.

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- If a property is held under trust, and such property is a business, the case would fall u/s 11(4) and not u/s 11(4A) of the Act. S.11(4A) of the Act, would apply only to a case where the business is not held under trust. There is a difference between a property or business held under trust and a business carried on by or on behalf of the trust.
- The interface between Ss 11(1) and (4) is of some importance. Firstly, u/s 11(4), it is only business which is held under trust that would enjoy exemption in respect of its income u/s 11(1). Secondly, there is a distinction between the objects of a trust and the powers given to the trustees to effectuate the purposes of the trust.
- A mere direction that the income from the business shall be applied to the charitable objects of a trust, without there being a settlement of the business itself upon trust, does not result in any trust or legal obligation.
- In *Thanthi Trust*'s case, the newspaper business was incidental to the attainment of the object of the trust, namely that of imparting education. This aspect is important, because the aim of the trust was a per se charitable object, not a GPU object. The observations were therefore made, having regard to the fact that the profits of the newspaper business were utilized by the trust for achieving the object of education. In the light of such facts, the carrying on of newspaper business, could be incidental to the object of education a per se category. The *Thanthi Trust* ratio therefore, cannot be extended to cases where the trust carries on business which is not held under trust and whose income is utilized to feed the charitable objects of the trust.

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- The journey which began with *Surat Art Silk* was interpreted in *Thanthi Trust* to mean that the carrying on of business by GPU charity was permissible as long as it inured to the benefit of the trust. The change brought about by the amendments in questions, however, place the focus on an entirely different perspective: that if at all any activity in the nature of trade, commerce or business, or a service in the nature of the same, for any form of consideration is permissible, that activity should be intrinsically linked to, or a part of the GPU category charity's object.
- Thus, the test of the charity being driven by a predominant object is no longer good law. Likewise, the ambiguity with respect to the kind of activities generating profit which could feed the main object and incidental profit-making also is not good law.
- What instead, the definition under S.2(15) through its proviso directs and thereby marks a departure from the previous law, is – firstly that if a GPU charity is to engage in any activity in the nature of trade, commerce or business, for consideration it should only be a part of this actual function to attain the GPU objective and, secondly and the equally important consideration, is the imposition of a quantitative standard - i.e., income (fees, cess or other consideration) derived from activity in the nature of trade, business or commerce or service in relation to these three activities, should not exceed the quantitative limits [Rs 10,00,000 (w.e.f. 1.4.2009), Rs 25,00,000 (w.e.f. 1.4.2012), and 20% (w.e.f. 1.4.2016)] of the total receipts. Lastly, the "ploughing" back of business income to "feed" charity is an irrelevant factor – again emphasizing the prohibition from engaging in trade, commerce or business.

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- If one understands the definition in the light of the above enunciation, the sequitur is that the reference to “income being profits and gains of business” with a further reference to its being incidental to the objects of the Trust, cannot and does not mean proceeds of activities incidental to the main object, incidental objects or income derived from incidental activities. The proper way of reading reference to the term “incidental” in S.11(4A) is to interpret it in the light of the sub-clause (i) of proviso to S.2(15), i.e., that the activity in the nature of business, trade, commerce or service in relation to such activities should be conducted actually in the course of achieving the GPU object, and the income, profit or surplus or gains can then, be logically incidental.
- Thus interpreted, there is no conflict between the definition of charitable purpose and the machinery part of S.11(4A). Further, the obligation under S.11(4A) to maintain separate books of account in respect of such receipts is to ensure that the quantitative limit imposed by sub-clause (ii) to S.2(15) can be computed and ascertained in an objective manner.
- Pure charity in the sense that the performance of an activity without any consideration is not envisioned under the Act. If one keeps this in mind, what S. 2(15) emphasizes is that so long as a GPU’s charity’s object involves activities which also generates profits (incidental, while actually carrying out the objectives of GPU, if some profit is generated), it can be granted exemption provided quantitative limit (of not exceeding 20%) under second proviso to S. 2(15) for receipts from such profits, is adhered to.

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- Another manner of looking at the definition together with S.s 10(23C) and 11 is that for achieving a general public utility object, if the charity involves itself in activities, that entail charging amounts only at cost or marginal mark up over cost, and also derive some profit, prohibition against carrying on business or service relating to business is not attracted - if quantum of such profits do not exceed 20% of its overall receipts.
- Illustrations where activities are not in nature of business
  - Gandhi Peace Foundation disseminating Mahatma Gandhi's philosophy through museums and exhibitions and publishing his works, for nominal cost is not business
  - providing access to low-cost hostels to weaker segments of society, where the fee or charges recovered cover the costs (including administrative expenditure) plus nominal mark up;
  - renting marriage halls for low amounts, again with a fee meant to cover costs;
  - blood bank services, again with fee to cover costs
- When the entity concerned charges substantial amounts over and above the cost it incurs for doing the same work, or work which is part of its object (i.e., publishing an expensive coffee table book on Gandhi, or in the case of the marriage hall, charging significant amounts from those who can afford to pay, by providing extra services, far above the cost-plus nominal markup) such activities are in the nature of trade, commerce, business or service in relation to them. In such case, the receipts from such latter kind of activities where higher amounts are charged, should not exceed the limit indicated by proviso (ii) to Section 2(15).

AUDA – Statutory Housing Boards, Regulatory Authorities & Corporations - Conclusions

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(i) The fact that bodies which carry on statutory functions whose income was eligible to be considered for exemption under Section 10(20A) ceased to enjoy that benefit after deletion of that provision w.e.f. 01.04.2003, does not ipso facto preclude their claim for consideration for benefit as GPU category charities, under Section 11 read with Section 2(15).

(ii) Statutory Corporations, Boards, Authorities, Commissions, etc. (by whatsoever names called) in the housing development, town planning, industrial development sectors are involved in the advancement of objects of general public utility, therefore are entitled to be considered as charities in the GPU categories.

(iii) Such statutory corporations, boards, trusts authorities, etc. may be involved in promoting public objects and also in the course of their pursuing their objects, involved or engaged in activities in the nature of trade, commerce or business.

(iv) The determinative tests to consider when determining whether such statutory bodies, boards, authorities, corporations, autonomous or self governing government sponsored bodies, are GPU category charities:

AUDA – Statutory Housing Boards, Regulatory Authorities & Corporations

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(a) Does the state or central law, or the MoA, constitution, etc. advance any GPU object, such as development of housing, town planning, development of industrial areas, regulation of any activity in the general public interest, supply of essential goods or services - such as water supply, sewage service, distributing medicines, food grains (PDS entities);
(b) While carrying on of such activities to achieve such objects (which are to be discerned from the objects and policy of the enactment; or in terms of the controlling instrument, such as MoA etc.), the purpose for which such public GPU charity, is set-up - whether for furthering the development or a charitable object or for carrying on trade, business or commerce or service in relation to such trade, etc.;
(c) Rendition of service or providing any article or goods, by such boards, authority, corporation, etc., on cost or nominal mark-up basis would not be activities in the nature of business, trade or commerce or service in relation to such business, trade or commerce;
(d) where the controlling instrument, particularly a statute imposes certain responsibilities or duties upon the concerned body, such as fixation of rates on pre-determined statutory basis, or based on formulae regulated by law, or rules having the force of law, recovery of such charges, fee, “fee, cess or other interest, etc. cannot be characterized as consideration” for engaging in activities in the nature of trade, commerce or business or for providing service in relation thereto;

AUDA – Statutory Housing Boards, Regulatory Authorities & Corporations

CNK

(e) Does the statute or controlling instrument set out the policy or scheme, for how the goods and services are to be distributed; in what proportion the surpluses, or profits, can be permissively garnered; are there are limits within which plots, rates or costs are to be worked out; whether the function in which the body is engaged in, is normally something a government or state is expected to engage in, having regard to provisions of the Constitution and the enacted laws, and the observations of this court in NDMC; whether in case surplus or gains accrue, the corporation, body or authority is permitted to distribute it, and if so, only to the government or state; the extent to which the state or its instrumentalities have control over the corporation or its bodies, and whether it is subject to directions by the concerned government, etc.;

(f) As long as the concerned statutory body, corporation, authority, etc. while actually furthering a GPU object, carries out activities that entail some trade, commerce or business, which generates profit (i.e., amounts that are significantly higher than the cost), and the quantum of such receipts are within the prescribed limit the concerned statutory or government organisations can be characterized as GPU charities.

AUDA – Statutory Regulatory Bodies, Authorities

CNK

- There are several other regulatory bodies that discharge functions which are otherwise within the domain of the State. A singular characteristic of ICAI and other statutory bodies which can be said to regulate specific functions and professions (including the profession of Cost and Work Accountants, and Company Secretary, etc.) is the powers conferred upon them by the statutes to prescribe standards and enforce them through disciplinary sanctions. Therefore, it is held that bodies which regulate professions and are created by/under statutes which are enjoined to prescribe compulsory courses to be undergone before the individual concerned is entitled to claim entry into the profession/vocation, and also continuously monitor conduct of its members do not ipso facto carry on activities in nature of trade, commerce or business, or services in relation thereto.
- It is important, at times, while considering the nature of activities (which may be part of a statutory mandate) that regulatory bodies may perform, whether the kind of consideration charged is vastly or significantly higher than the costs it incurs. For instance, there can be regulatory fees which may have to be paid annually, or the body may require candidates, or professionals to purchase and fill forms for entry into the profession, or towards examinations. If the level of such fees or collection are significantly higher than the cost, such income would attract the mischief of proviso to S. 2(15), and would have to be within the limits prescribed by sub-clause (ii) of proviso to S.2(15).

AUDA – Statutory Regulatory Bodies, Authorities

CNK

- Authorities set up under the Seeds Act, 1966 are set up as societies under Section 8 of the Seeds Act, and comprise of farmers, farmers cooperatives' representatives, seed certification authorities, etc. The task of these agencies and authorities is certification of seeds, to decide whether to certify supply of seeds of "any notified kind or variety", by applicants who may wish to offer them for trade. These agencies/authorities scrutinize the samples to ensure they conform to the requisite standard notified under Section 6.
- The functioning of the seed certification agency, is a crucial one, in those only seeds conforming to prescribed standards, are permitted to be traded and used, by farmers. Such standards are - in the context of the fact that agriculture is one of the mainstays of the economy, and furthermore, pivotal for food security - essential as they ensure efficacy of seeds and guarantee to the farmers that they can be relied upon. The essential nature of the regulatory function performed by these certification agencies is obvious. The nature of their activities is not by way of trade, commerce or business, nor service in relation to trade commerce, business, for some form of consideration.

AUDA – Trade Promotion bodies, councils, associations or organisations

CNK

- The change in definition in Section 2(15) and the negative phraseology has made a difference. Organizing meetings, disseminating information through publications, holding awareness camps and events, would be broadly covered by trade promotion. However, when a trade promotion body provides individualized or specialized services - such as conducting paid workshops, training courses, skill development courses certified by it, and hires venues which are then let out to industrial, trading or business organizations, to promote and advertise their respective businesses, the claim for GPU status needs to be scrutinised more closely. Such activities are in the nature of services "in relation to" trade, commerce or business. These activities, and the facility of consultation, or skill development courses, are meant to improve business activities, and make them more efficient. The receipts from such activities clearly are 'fee or other consideration' for providing service "in relation to" trade, commerce or business.
- APEC – it cannot be said that AEPC's functioning does not involve any element of trade, commerce or business, or service in relation thereto. Though in some instances, the recipient may be an individual business house or exporter, there is no doubt that these activities, performed by a trade body continue to be trade promotion. Therefore, they are in the "actual course of carrying on" the GPU activity. In such a case, for each year, the question would be whether the quantum from these receipts, and other such receipts are within the limit prescribed by the sub-clause (ii) to proviso to Section 2(15). If they are within the limits, AEPC would be – for that year, entitled to claim benefit as a GPU charity.

AUDA – Non-statutory bodies - ERNET

CNK

- ERNET is a not-for profit society, set up under the aegis of the Union Government.
- ERNET's networks are a mix of terrestrial and satellite-based wide-area network. It provides services through its 15 Points of Presence (PoPs) located across the country. All those are equipped to provide access to Intranet, Internet and Digital Library through trial leased circuits and radio links to the user institutions. …ERNET provides, services, namely, Network Access Services, Network Applications Services, Hosting Services, Operations Support Services and Domain Registration Services under srnet.in, ac.in, edu.in & res.in domains. Funded through government grants, its projects support educational networks and development of internet infrastructure in numerous other segments of society.
- Having regard to the nature of ERNET's activities, it cannot be said that they are in the nature of trade, commerce or business, or service, towards trade, commerce or business. It has to receive fees, to reimburse its costs. The materials on record nowhere suggest that its receipts (in the nature of membership fee, connectivity charges, data transfer differential charges, and registration charges) are of such nature as to be called as fees or consideration towards business, trade or commerce, or service in relation to it. The functions ERNET performs are vital to the development of online educational and research platforms.

AUDA – Non-statutory bodies - NIXI

CNK

- National Internet Exchange of India (NIXI) was established in 2003 under the aegis of the Ministry of Information Technology of the Union Government for the promotion and growth of internet services in India, to regulate the internet traffic, act as an internet exchange, and undertake ".in" domain name registration.
- Its object is to promote the interests of internet service providers and internet consumers in India, improve quality of internet service, save foreign exchange, and carry on domain name operations. It is bound by licensing conditions – which include the prohibition from altering its memorandum, without the prior consent of the Union Government.
- It is evident that NIXI carries on the essential – crucial purpose of promoting internet services and more importantly, regulating domain name registration which is extremely essential for internet users in India. A country's need to have a domestic internet exchange, rather than depend on an international one, cannot be overemphasized. The Union Government's object of setting up of internet exchange is part of its essential function as a government to regulate certain segment of the communication networks.
- Revenue's contention that NIXI does not merely carry-on public purpose of regulatory activity but is involved in trade, commerce, or business or in providing service in relation thereto, cannot be accepted.

AUDA – Non-statutory bodies – GS1 India

CNK

- GS1 codes were developed and created by GS1 International, Belgium (an international not-for-profit under Belgium tax law). This coding system has been in use worldwide and is even mandatory for some services/goods, or adopted for significant advantages being a singular identification system, recognized and accepted all over the world. The code promotes universal standard in Electronic Data Inter-exchanged (EDI) and other services. This system of coding has been accorded priority by the Government of India as it is a compulsory requirement on products exported from India.
- GS1 was set up as society in 1996 and sponsored by the Union Government. The Union Government representatives and the representatives of the trade bodies are its members.
- GS1's functions no doubt is of general public utility. However, equally the services it performs are to aid businesses, manufacturers, tradesmen and commercial establishments. Bar coding packaged articles and goods assists their consigners to identify them; helps manufacturers, and marketing organizations (especially in the context of contemporary times, online platforms which serve as market places). The objective of GS1 is therefore, to provide service in relation to business, trade or commerce - for a fee or other consideration. It is also true, that the coding system it possesses and the facilities it provides, is capable of and perhaps is being used, by other sectors, in the welfare or public interest fields. The materials on record show that the coding services are used for commercial or business purposes.

AUDA – State Cricket Associations

CNK

- The objects are to control, supervise, regulate, promote or encourage, and develop the game of cricket in the area under its jurisdiction. The association can also undertake any other and all activities which may be beneficial to it.
- There is no doubt that the claim of the present sport associations will not fall within 'education' and will have to be examined under the fourth limb of Section 2(15) i.e., GPU category, if it is to make a case for tax exemption.
- As things stand, therefore, the state associations and BCCI are linked closely. The management of the game of cricket is structured in such a way that this link is apparent at every match or fixture of significance. In the course of conducting matches (which are scheduled by the BCCI as the national co-ordinating body), apart from amounts received towards sale of entry tickets, the state associations also receive advertisement money, sponsorship fee, etc. from the BCCI. Aside from these, media rights - i.e., broadcasting rights to each national or international event conducted at various locales owned by the state associations, and digital rights (all of which are exclusive, in nature) – are auctioned by BCCI. As noticed above, the BCCI, by its own admission, negotiates the terms on which media rights are sold, on behalf of the state associations
- Only a fraction of income has been expended towards promotion of cricket

AUDA – State Cricket Associations

CNK

- It is quite evident that the activities of the cricket associations are run on business lines. The associations own physical and other infrastructure, maintain them, have arrangements for permanent manpower and have well-organized supply chains to cater to the several matches they host. Many such matches are not at national level and are under-16 or under-18 matches at the regional level. However, these activities are not to be seen in isolation but are to be regarded as part of the overall scheme, and ecosystem in which the game of cricket is organized in India. Talent is spotted, at local levels and dependent on the promise shown, given appropriate exposure.
- On a close scrutiny of the expenses borne, having regard to the nature of receipts, the expenditure incurred by Cricket Associations does not disclose that any significant proportion is expended towards sustained or organized coaching camps or academies. Therefore, in the opinion of this court, the ITAT fell into error in not considering the nature of receipts flowing from the BCCI into the corpus of GCA and SCA – as well as other associations that are before this court to determine their true character. The ITAT appears to have been swayed by the submission that the amount given by the BCCI were towards capital subsidy.
- Recent trends have shown that media rights, especially broadcasting and digital media rights have yielded colossal revenues to the BCCI. As discussed previously, these media rights are not per se owned by BCCI, which is but an association of persons or agglomerate of all the State Cricket Association. The stadia which form the venue for these cricket matches (in relation to which media rights are transferred or licensed) are owned by the State Cricket Associations. According to the BCCI itself, the State Associations can well bargain and enter into arrangements for the sale of such media rights.

AUDA – State Cricket Associations

CNK

- However, to obtain better terms, and gain bargaining leverage a centralized form of sale of such rights has been agreed and adopted by which the BCCI auctions these rights on behalf of the State Associations. All State Associations put together are entitled to 70% of the revenue i.e., the proceeds of sale of the media rights. This may or may not be in proportion to the events hosted by each or some of the cricket associations. Yet, this forms part of the arrangement by which the consideration flowing from such commercial rights has been agreed to be shared amongst all members of the BCCI. These rights are apparently commercial.
- The High Court fell into error in accepting at face value the submission that the amounts made over by BCCI to the cricket associations were in the nature of infrastructure subsidy.
- In each case, and for every year, the tax authorities are under an obligation to carefully examine and see the pattern of receipts and expenditure. Whilst doing so, the nature of rights conveyed by the BCCI to the successful bidders, in other words, the content of broadcast rights as well as the arrangement with respect to state associations (either in the form of master documents, resolutions or individual agreements with state associations) have to be examined.

AUDA – Conclusions

CNK

General Test u/s 2(15)

- An assessee advancing general public utility cannot engage itself in any trade, commerce or business, or provide service in relation thereto for any consideration ("cess, or fee, or any other consideration");
- However, in the course of achieving the object of general public utility, the concerned organization can carry on trade, commerce or business or provide services in relation thereto for consideration, provided that

  (i) the activities of trade, commerce or business are connected ("actual carrying out…" inserted w.e.f. 01.04.2016) to the achievement of its objects of GPU; and

  (ii) the receipt from such business or commercial activity or service in relation thereto, does not exceed the quantified limit, as amended over the years
- Generally, the charging of any amount towards consideration for such an activity (advancing general public utility), which is on cost-basis or nominally above cost, cannot be considered to be "trade, commerce, or business" or any services in relation thereto. It is only when the charges are markedly or significantly above the cost incurred by the assessee in question, that they would fall within the mischief of "cess, or fee, or any other consideration" towards "trade, commerce or business".
- Clarified through illustrations what kind of services or goods provided on cost or nominal basis would normally be excluded from the mischief of trade, commerce, or business

AUDA – Conclusions

CNK

General Test u/s 2(15)

- S.11(4A) must be interpreted harmoniously with S.2(15), with which there is no conflict. Carrying out activity in the nature of trade, commerce or business, or service in relation to such activities, should be conducted in the course of achieving the GPU object, and the income, profit or surplus or gains must, therefore, be incidental. The requirement in S. 11(4A) of maintaining separate books of account is also in line with the necessity of demonstrating that the quantitative limit prescribed in the proviso to S.2(15), has not been breached. Similarly, the insertion of Section 13(8), seventeenth proviso to S. 10(23C) and third proviso to S.143(3) (all w.r.e.f. 01.04.2009), reaffirm this interpretation and bring uniformity across the statutory provisions.

Authorities, corporations, or bodies established by statute

- The amounts or any money whatsoever charged by a statutory corporation, board or any other body set up by the state/central governments, for achieving what are essentially 'public functions/services' (such as housing, industrial development, supply of water, sewage management, supply of food grain, development and town planning, etc.) may resemble trade, commercial, or business activities. However, since their objects are essential for advancement of public purposes/functions (and are accordingly restrained by way of statutory provisions), such receipts are prima facie to be excluded from the mischief of business or commercial receipts. This is in line with the larger bench judgments of this court in Ramtanu Cooperative Housing Society and NDMC.

AUDA – Conclusions

CNK

- However, at the same time, in every case, the assessing authorities would have to apply their minds and scrutinize the records, to determine if, and to what extent, the consideration or amounts charged are significantly higher than the cost and a nominal mark-up. If such is the case, then the receipts would indicate that the activities are in fact in the nature of “trade, commerce or business” and as a result, would have to comply with the quantified limit (as amended from time to time) in the proviso to Section 2(15)
- In clause (b) of Section 10(46) of the IT Act, “commercial” has the same meaning as “trade, commerce, business” in Section 2(15). Therefore, sums charged by such notified body, authority, Board, Trust or Commission (by whatever name called) will require similar consideration – i.e., whether it is at cost with a nominal mark-up or significantly higher, to determine if it falls within the mischief of “commercial activity”. However, in the case of such notified bodies, there is no quantified limit in Section 10(46). Therefore, the Central Government would have to decide on a case-by-case basis whether and to what extent, exemption can be awarded to bodies that are notified under Section 10(46).
- For the period 01.04.2003 to 01.04.2011, a statutory corporation could claim the benefit of Section 2(15) having regard to the judgment of this Court in the Gujarat Maritime Board case (supra). Likewise, the denial of benefit under Section 10(46) after 01.04.2011 does not preclude a statutory corporation, board, or whatever such body may be called, from claiming that it is set up for a charitable purpose and seeking exemption under Section 10(23C) or other provisions of the Act.

AUDA – Conclusions

CNK

Statutory regulators

- The income and receipts of statutory regulatory bodies which are for instance, tasked with exclusive duties of prescribing curriculum, disciplining professionals and prescribing standards of professional conduct, are prima facie not business or commercial receipts.
- However, this is subject to the caveat that if the assessing authorities discern that certain kinds of activities carried out by such regulatory body involved charging of fees that are significantly higher than the cost incurred (with a nominal mark-up) or providing other facilities or services such as admission forms, coaching classes, registration processing fees, etc., at markedly higher prices, those would constitute commercial or business receipts.
- In that event, the overall quantitative limit prescribed in the proviso to Section 2(15) (as amended from time to time) has to be complied with, if the regulatory body is to be considered as one with ‘charitable purpose’ eligible for exemption.
- Like statutory authorities which regulate professions, statutory bodies which certify products (such as seeds) based on standards for qualification, etc. will also be treated similarly.

AUDA – Conclusions

CNK

Trade Promotion Bodies

- Bodies involved in trade promotion (such as AEPC), or set up with the objects of purely advocating for, coordinating and assisting trading organisations, can be said to be involved in advancement of objects of general public utility. However, if such organisations provide additional services such as courses meant to skill personnel, providing private rental spaces in fairs or trade shows, consulting services, etc. then income or receipts from such activities, would be business or commercial in nature. In that event, the claim for tax exemption would have to be again subjected to the rigors of the proviso to Section 2(15) of the IT Act.

Non-Statutory Bodies

- In the present batch of cases, non-statutory bodies performing public functions, such as ERNET and NIXI are engaged in important public purposes. The materials on record show that fees or consideration charged by them for the purposes provided are nominal. In the circumstances, it is held that the said two assessees are driven by charitable purposes. However, the claims of such non-statutory organisations performing public functions, will have to be ascertained on a yearly basis, and the tax authorities must discern from the records, whether the fees charged are nominally above the cost, or have been increased to much higher levels.

AUDA – Conclusions

CNK

Non-Statutory Bodies

- Though GS1 India is in fact, involved in advancement of general public utility, its services are for the benefit of trade and business, from which they receive significantly high receipts. In the circumstances, its claim for exemption cannot succeed having regard to amended Section 2(15). However, the Court does not rule out any future claim made and being independently assessed, if GS1 is able to satisfy that what it provides to its customers is charged on cost-basis with at the most, a nominal markup.

Sports associations

- The matter requires further scrutiny - AO shall adjudicate the matter afresh after issuing notice to the concerned assessees and examining the relevant material indicated

Private Trusts

- Tribune Trust - despite advancing general public utility, the Trust cannot benefit from exemption offered to entities covered by Section 2(15) as the records reveal that income received from advertisements, constituted business or commercial receipts. Consequently, the limit prescribed in the proviso to Section 2(15) has to be adhered to for the Trust's claim of being as a charity eligible for exemption, to succeed. Therefore, despite differing reasoning, this court has held that the impugned judgment of the High Court does not call for interference.

AUDA – Conclusions

CNK

- The conclusions arrived at by way of this judgment, neither precludes any of the assessees (whether statutory, or non-statutory) advancing objects of general public utility, from claiming exemption, nor the taxing authorities from denying exemption, in the future, if the receipts of the relevant year exceed the quantitative limit. The assessing authorities must on a yearly basis, scrutinize the record to discern whether the nature of the assessee's activities amount to "trade, commerce or business" based on its receipts and income (i.e., whether the amounts charged are on cost-basis, or significantly higher). If it is found that they are in the nature of "trade, commerce or business", then it must be examined whether the quantified limit (as amended from time to time) in proviso to Section 2(15), has been breached, thus disentitling them to exemption.
- Clarification sought by Revenue – order dated 3 Nov 2022
- Application of law declared – apply for assessment years in question which were before this court, and were decided
- Wherever appeals decided against the revenue, they are to be treated as final
- For AYs which the Court was not called upon to decide, concerned authorities will apply the law declared in this judgment, having regard to the facts of each such AY

AUDA – Issues

CNK

- Does every high surplus activity amount to trade, commerce or business? E.g. interest, rent
- What percentage is meant by “significantly higher than cost”?
- What expenses form part of cost?
  - Capital Expenditure or Depreciation
  - Write offs
  - Notional cost of voluntary service?
- What if the high surplus is due to large volumes, though fee is nominal?
- What if surplus arises due to grants, or due to interest income?
- If objects are medical, educational, relief of poverty, etc and not GPU, and substantial surplus arises from main activity, applicability of the decision
- If incidental business means charitable activity itself, how does one maintain separate accounts where there is no other activity?
- What is the position regarding fund-raising activities, such as music concerts, film shows, auction of paintings, etc?


Thank
you