

Denial of exemption under section 11, in view of violation of section 13

[Denial of exemption under section 11 to the total income of a trust, in view of violation of section 13(1)(c) / 13(1)(d), is not legally tenable]

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Section 11 of the Income-Tax Act, 1961 (the Act) excludes from the income of charitable or religious trusts, income to the extent it is applied towards the objects of such trusts, during the previous year in India. It may be stated here that there are several conditions laid down under section 11 of the Act, for the purpose of claiming exemption in respect of the income of a charitable or religious trust.

As regards the exemption available under section 11 of the Act, the provisions of section 13 are quite relevant. The heading of section 13 is “*Section 11 not to apply in certain cases*”. In other words, section 13 provides that exemption under section 11 will not be available in cases of violation of the provisions of section 13 of the Act.

Most of the violations under section 13 of the Act fall under section 13(1)(c) of the Act, whereas few violations also fall under section 13(1)(d) of the Act. Besides, section 13(2) lists conditions which are deemed to be violation under sections 13(1)(c) or 13(1)(d). These provisions may briefly be explained as follows :

(i) Section 13(1)(c) – Benefit to interested persons

Section 13(1)(c) of the Act has carved out an exception from exemption in cases where a part of income of a charitable or religious trust / institution enures or is used or applied directly or indirectly for the benefit of the settlor, founder or certain other specified persons under section 13(3) of the Act. This is obviously intended to ensure that the income of such a trust / institution is not diverted towards the benefit of persons who are closely connected with the creation, establishment and conduct of the affairs of the trust / institution.

(ii) Section 13(1)(d) – Investment of funds of the trust / institution in modes or forms other than those specified.

Section 13(1)(d) provides that exemption from tax to charitable or religious trust / institution will be forfeited if any funds of the trust / institution are invested or deposited after 28.2.1983, otherwise than in any one or more of the forms or modes specified therein.

(iii) Section 13(2) – Bar due to deemed use / application of the income or property of the trust by interested persons.

As per section 13(2) of the Act, without prejudice to the generality of the provisions of section 13(1)(c) and section 13(1)(d), the income or the property of the trust or institution or any part of such income or property shall, for the purposes of that clause, be deemed to have been used or applied for the benefit of persons referred to in section 13(3), in situations listed under clauses (a) to (h) thereof.

Thus, the provisions of section 13(2) are nothing but extension of the provisions of section 13(1)(c) / 13(1)(d) of the Act.

As regards denial of exemption under section 11, in respect of total income of a trust / institution, because of misuse of income or property of the trust by the interested persons, there have been bizarre instances. In such instances, a very insignificant use of the income / property by a trustee, has been held to be a violation of section 13(1)(c) and as a result thereof, exemption under section 11 of the Act has been denied to the total income of the trust / institution. One such instance is provided by the judgement of Kerala High Court, in the case of *Agappa Child Centre Vs CIT [1997] 226 ITR 211 (Ker)*. In this case, the trust purchased a refrigerator for its own use. However, before the completion of the trust buildings, the trust kept the said refrigerator at the residence of the managing trustee of the trust. The ITO refused exemption to the trust under section 11 of the Act, on the ground that use of refrigerator by the managing trustee was violation of the provisions of section 13(2)(b) of the Act. The aforesaid conclusion of the AO was upheld by the CIT(A), the Tribunal, as well as the High Court.

Besides, I know a number of cases where an educational institution running a number of professional colleges, as well as other colleges, incurred expenditure on the foreign tour of the managing trustee, which was undertaken purely for the purposes of the objects of the trust. The expenditure incurred on such a tour might not be more than Rs.5 lakhs. However, the Assessing Officer took a very perverted view to the effect that the aforesaid tour was nothing but a pleasure trip on the part of the managing trustee. As a result, the aforesaid foreign tour was treated as a violation of the provisions of section 13(1)(c) of the Act and consequently the educational institution was denied the benefit of exemption under section 11. Accordingly, the income of the institution running into several hundred cores was brought to tax. The aforesaid action of the AO for a number of assessment years has totally ruined the financial health of the institution.

It has been my considered view that the aforesaid approach on the part of the I.T. Department is not in accordance with the intended purpose of the provisions of section 13(1)(c), 13(1)(d) or 13(2) of the Act.

My aforesaid view has received support from the recent judgement of Karnataka High Court, in the case of *CIT Vs Fr.Mullers Charitable Institutions [2014] 363 ITR 230 (Karn)*. It was held in this case that perusal of section 13(1)(d) of the Act, makes it clear that it is only the income from such investment or deposit, which has been made in violation of section 11(5) of the Act, that is liable to be taxed and violation of section 13(1)(d) does not result in denial of exemption under section 11 to the total income of the assessee trust.

The aforesaid judgement of Karnataka High Court is based on the judgement of Bombay High Court, in the case of *DIT(E) Vs.Sheth Mafatlal Gagalbhai Foundation Trust [2001] 249 ITR 533 (Bom)*.

In the present context, the provisions of section 164, particularly section 164(2) and proviso thereto, are also relevant. It may also be stated here that in view of the proviso to section 164(2) and Circular No.387, dt.6.7.1984, issued by the CBDT, all the legal precedents applicable to the violations under section 13(1)(d) of the Act, will equally apply to the violations under section 13(1)(c) of the Act.

Before proceeding to deal with the relevant legal precedents in support of the aforesaid stand, it would be appropriate to refer to the relevant provisions of sections 13 and 164 of the Act, along with relevant Circular of the CBDT. The same are discussed as follows :

I. Sections 13(1)(c), 13(1)(d) and 13(2) of the Act.

In the present context, the provisions of sections 13(1)(c), 13(1)(d) and 13(2) of the Act, are relevant. The same are discussed as follows :

1. Provisions of sections 13(1)(c) of the Act

For the sake of ready reference, the relevant part of section 13(1)(c) of the Act, is reproduced as follows :

“13. Section 11 not to apply in certain cases.

(1) Nothing contained in section 11 or section 12 shall operate so as to exclude from the total income of the previous year of the person in receipt thereof—

(c) in the case of a trust for charitable or religious purposes or a charitable or religious institution, any income thereof—

(i) if such trust or institution has been created or established after the commencement of this Act and under the terms of the trust or the rules governing the institution, any part of such income enures, or

(ii) if any part of such income or any property of the trust or the institution (whenever created or established) is during the previous year used or applied,

directly or indirectly for the benefit of any person referred to in sub-section (3) :”

From the aforesaid provisions of section 13(1)(c)(ii), it may be seen that if any part of income or any property of the trust is applied directly or indirectly for the benefit of any trustee, etc, then the benefit of exemption under section 11 of the Act, will not be available to the trust, **in respect of such income.**

2. Provisions of section 13(1)(d) of the Act.

For the sake of ready reference, the relevant part of section 13(1)(d) of the Act, is reproduced as follows :

“13. Section 11 not to apply in certain cases.

(1) Nothing contained in section 11 or section 12 shall operate so as to exclude from the total income of the previous year of the person in receipt thereof—

(d) in the case of a trust for charitable or religious purposes or a charitable or religious institution, any income thereof, if for any period during the previous year—

(i) any funds of the trust or institution are invested or deposited after the 28th day of February, 1983 otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11; or

(ii) any funds of the trust or institution invested or deposited before the 1st day of March, 1983 otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11 continue to remain so invested or deposited after the 30th day of November, 1983; or

(iii) any shares in a company, other than—

(A) shares in a public sector company ;

(B) shares prescribed as a form or mode of investment under clause (xii) of sub-section (5) of section 11,

are held by the trust or institution after the 30th day of November, 1983:”

From the aforesaid provisions of section 13(1)(d), it may be seen that if the conditions laid down there under are not fulfilled, then the trust will lose the benefit of exemption under section 11 of the Act, **in respect of income referred to therein.**

3. Provisions of section 13(2) of the Act.

In the present context, section 13(2) of the Act is also relevant. For the sake of ready reference, section 13(2) of the Act, is reproduced as follows :

“13. Section 11 not to apply in certain cases.

(2) Without prejudice to the generality of the provisions of clause (c) and clause (d) of sub-section (1), the income or the property of the trust or institution or any part of such income or property shall, for the purposes of that clause, be deemed to have been used or applied for the benefit of a person referred to in sub-section (3),—

(a) if any part of the income or property of the trust or institution is, or continues to be, lent to any person referred to in sub-section (3) for any period during the previous year without either adequate security or adequate interest or both;

(b) if any land, building or other property of the trust or institution is, or continues to be, made available for the use of any person referred to in sub-section (3), for any period during the previous year without charging adequate rent or other compensation;

(c) if any amount is paid by way of salary, allowance or otherwise during the previous year to any person referred to in sub-section (3) out of the resources of the trust or institution for services rendered by that person to such trust or institution and the amount so paid is in excess of what may be reasonably paid for such services;

(d) if the services of the trust or institution are made available to any person referred to in sub-section (3) during the previous year without adequate remuneration or other compensation;

(e) if any share, security or other property is purchased by or on behalf of the trust or institution from any person referred to in sub-section (3) during the previous year for consideration which is more than adequate;

(f) *if any share, security or other property is sold by or on behalf of the trust or institution to any person referred to in sub-section (3) during the previous year for consideration which is less than adequate;*

(g) *if any income or property of the trust or institution is diverted during the previous year in favour of any person referred to in sub-section (3):*

Provided *that this clause shall not apply where the income, or the value of the property or, as the case may be, the aggregate of the income and the value of the property, so diverted does not exceed one thousand rupees;*

(h) *if any funds of the trust or institution are, or continue to remain, invested for any period during the previous year (not being a period before the 1st day of January, 1971), in any concern in which any person referred to in sub-section (3) has a substantial interest.”*

From the aforesaid provisions of section 13(2), it may be seen that in respect of various circumstances referred to in clauses (a) to (h) thereof, the income or property of the trust or institution or any part of such income or property shall, for the purposes of section 13(1)(c) and 13(1)(d), be deemed to have been used or applied for the benefit of the trustee, etc. It clearly implies that section 13(2) is nothing but an extension of section 13(1)(c) / 13(1)(d).

II. Section 164(2) of the Act.

In the present context, the provisions of section 164(2) are also relevant, which are reproduced as follows :

“164.Charge of tax where share of beneficiaries unknown.

(2) *In the case of relevant income which is derived from property held under trust wholly for charitable or religious purposes, or which is of the nature referred to in sub-clause (iia) of clause (24) of section 2 or which is of the nature referred to in sub-section (4A) of section 11 tax shall be charged on so much of the relevant income as is not exempt under section 11 or section 12, as if the relevant income not so exempt were the income of an association of persons :*

Provided *that in a case where the whole or any part of the relevant income is not exempt under section 11 or section 12 by virtue of the provisions contained in clause (c) or clause (d)*

of sub-section (1) of section 13, tax shall be charged on the relevant income or part of relevant income at the maximum marginal rate.”

From the aforesaid provisions of section 164(2), it may be seen that in the case of relevant income referred to therein, tax shall be charged on so much of the relevant income, as is not exempt under section 11 or 12, as if the relevant income not so exempt were the income of an association of persons (AOP). It clearly implies that only that part of the relevant income which is not exempt under section 11 or section 12 is brought to tax, as the income of an AOP and the balance of income of the charitable trust / institution, will remain exempt.

Further, as per the proviso to section 164(2), where the whole or any part of the relevant income is not exempt under section 11 or section 12, by virtue of the provisions of section 13(1)(c) or section 13(1)(d), tax shall be charged on the relevant income or part of relevant income, at the maximum marginal rate.

In view of the aforesaid proviso to section 164(2), the Courts have held that in case of violation of the conditions under section 13(1)(c) or 13(1)(d) of the Act, only the relevant income or part of such relevant income is liable to be taxed at maximum marginal rate. It is also held that the violation of section 13(1)(c) or 13(1)(d) does not result in denial of exemption under section 11, in respect of the total income of the assessee. In other words, only the non-exempt income, in view of the provisions of section 13(1)(c) / 13(1)(d) would fall in the tax-net and the other income of the charitable trust / institution would remain exempt under the provisions of section 11 of the Act.

III. Relevant part of Circular No.387, dt.6.7.1984 [152 ITR (St) 1].

In the present context, paragraph 28 of Circular No.387, dt.6.7.1984, issued by the CBDT, under the heading “*Levy of income-tax at maximum marginal rate in the case of charitable and religious trusts which forfeit tax exemption*” is very relevant. For our purpose, paragraph 28.6 of the aforesaid Circular is relevant, which is reproduced as follows :

“28.6 It may be noted that new sub-section (1A) inserted in section 161 of the IT Act, which provides for taxation of the entire income received by trusts at the maximum marginal rates is applicable only in the case of private trusts having profits and gains of business. So far as public charitable and religious trusts are concerned, their business profits are not exempt from tax, except in the cases falling under clause (a) or clause (b) of section 11(4A) of the IT Act. As the maximum marginal rate of tax under the new proviso to section 164(2) applies to the whole or a part of the relevant income of a charitable or religious trust which forfeits

exemption by virtue of the provisions of the IT Act in regard to investment pattern or use of the trust property for the benefit of the settlor, etc., contained in section 13(1)(c) and (d) of that Act, the said rate will not apply to the business profits of such trusts which are otherwise chargeable to tax. In other words, where such a trust contravenes the provisions of section 13(1)(c) or (d) of the Act, the maximum marginal rate of income-tax will apply only to that part of the income which has forfeited exemption under the said provisions.”

As per the aforesaid paragraph 28.6 of the aforesaid Circular, where such a trust contravenes the provisions of section 13(1)(c) or 13(1)(d) of the Act, the maximum marginal rate of income-tax will apply only to that part of income, which has forfeited exemption under the said provisions.

From the aforesaid discussion, it is clearly established that a legal precedent which applies in relation to violation of the provisions of section 13(1)(d), will equally apply in relation to violation of the provisions of section 13(1)(c), also.

IV. The relevant legal precedents

There are a number of legal precedents in support of the aforesaid stand, including the aforesaid judgements of Karnataka and Bombay High Courts. The same are discussed as follows:

1. CIT Vs Fr.Mullers Charitable Institutions [2014] 363 ITR 230 (Karn)

In this case, the assessee, a charitable trust, for the AYs 2000-01 and 2001-02 claimed exemption under section 11. The AO noticed that the assessee had advanced a sum of Rs.30 lakhs during the AY 2000-01 and a sum of Rs.50 lakhs during the AY 2001-02, respectively, to a company which was running a Kannada daily. According to the AO, advancing of such a huge amount was in violation of section 11(5). Further, as per section 13(1)(d), the trust shall not be entitled for exemption under sections 11 and 12 of the Act. Accordingly, the AO assessed the aforesaid advances to tax.

However, the CIT was of the opinion that in view of violation of section 11(5), the entire income of the trust ought to have been assessed, as the trust was not entitled to any exemption under sections 11 and 12 of the Act and the CIT revised the order passed by the AO.

On appeal, the Tribunal, after considering the matter in detail and on examining sections 11, 12, 13(1)(d) and section 164(2) of the Act, *inter alia*, held that the order passed by the CIT was contrary to section 164(2) of the Act and the entire income of the assessee could not be assessed.

On appeal by the Revenue before the High Court, one of the substantial question of law admitted was whether the Tribunal was correct in holding that when a part of income is held to be violative of the provisions of section 13(1)(d), only to the said extent, maximum marginal rate of tax is to be levied and not for the whole income, more particularly when there was violation of the provisions of section 11(5) of the Act. **It was held by the High Court that a reading of section 13(1)(d) of the Act, makes it clear that it is only the income from such investment or deposit which has been made in violation of section 11(5) of the Act, that is liable to be taxed and that the violation of section 13(1)(d) does not tantamount to denial of exemption under section 11 to the total income of the assessee. Accordingly, the appeals of the IT Department were dismissed.**

In the aforesaid case, the Karnataka High Court has placed reliance on the judgement of the Bombay High Court, in the case of *DIT(E) Vs Sheth Mafatlal Gagalbhai Foundation Trust [2001] 249 ITR 533 (Bom)*. Besides, a reference has also been made to the judgement of Delhi High Court, in the case of *DIT(E) Vs Agrim Charan Foundation [2002] 253 ITR 593 (Del)*. In this context, the following observations of the Hon. High Court, on page 238 of the Report are very relevant :

*“We are in respectful agreement that the views expressed by the Bombay High Court as well as the Delhi High Court for violating section 11(5) of the Act and **the entire income of the Respondent trust cannot be assessed for the tax**”* [Emphasis added]

Thus, it was made very clear that where the whole or part of the relevant income is not exempted under section 11, by virtue of violation of section 13(1)(d) of the Act, tax shall be levied on the relevant income or part of the relevant income, at the maximum marginal rate. However, violation of section 13(1)(d) does not result in the denial of exemption under section 11, to the total income of the assessee.

2. *DIT(E) Vs Sheth Mafatlal Gagalbhai Foundation Trust [2001] 249 ITR 533 (Bom).*

In this case, according to the AO, on account of violation of section 11(5) of the Act, the assessee forfeited exemption under section 11, in respect of its entire income, viz. dividend income plus interest income, whereas according to the assessee, they were entitled to claim exemption and they were entitled to continuance of exemption in respect of interest income, though they had forfeited the right to claim exemption vis-a-vis the dividend income, as the assessee continued to hold the shares in a non-Government company even after 31.3.1993. On appeal, the CIT(A) came to the conclusion that the assessee was not entitled to the benefit of exemption under section 11, in respect of the entire income.

On further appeal, the Tribunal came to the conclusion that in view of section 164(1), the income receivable by the trust was the relevant income. That a portion of such relevant income only would suffer tax because of the violation of the condition of investment prescribed under section 11(5). The Tribunal found that non-fulfilment of such condition could not deprive the trust of the exemption of its other income, which had been granted to it in the earlier years. Hence, the Tribunal allowed the appeal of the assessee.

Against the aforesaid judgement of the Tribunal, an appeal was filed by the Department before the High Court. The following question was raised before the Hon.High Court :

“Whether violation of section 11(5), r.w.s.13(1)(d), by the assessee trust attracts maximum marginal rate of tax on the entire income of the trust”.

The Counsel of the IT Department contended that in view of section 164(2), the forfeiture of exemption for breach of section 11(5) would result in imposition of tax on the maximum marginal rate, as if the assessee was an association of persons (AOP). He further contended that the entire income of the Trust was liable to be charged to tax under maximum marginal rate, on the basis of such income accruing to an association of persons.

On the other hand, the Counsel for the assessee contended that the requirement of investment for specified securities under section 11(5) results in an income to the trust which is receivable by the trustees and it is called **relevant income under section 164(1)**. He further contended that a portion of such relevant income in the present case would suffer tax because the condition of investment as prescribed under section 11(5) had not been fulfilled. But non-

fulfilment of such condition could not deprive the trust of the exemption of its other income, which had been granted in earlier years. He further contended that in this connection, the proviso to section 164(2) is very important. According to him, the Legislature has clearly contemplated that in a case where the whole or part of the relevant income is not exempt under section 11, by virtue of violation of section 13(1)(d), tax shall be charged on the relevant income or part of the relevant income at the maximum marginal rate. In this connection, he also relied upon Circular No.387, dt.6.7.1984, issued by the CBDT [152 ITR (St) 1].

It was held by the High Court that section 164(2) refers to the relevant income which is derived from property held under trust wholly for charitable or religious purposes. **If such income consists of severable portions, exempt as well as taxable, the portion which is exempt is to be left out and the portion which is not exempt is charged to tax as if it is the income of the association of persons.** Therefore, a proviso was inserted by the Finance Act, 1984, with effect from 1.4.1985, under which in cases where the whole or any part of the relevant income is not exempt under section 11 or section 12, because of the contravention of section 13(1)(d), then tax shall be charged on such income or part thereof, as the case may be, at the maximum marginal rate. **In other words, only non-exempt income portion would fall in the net of tax, as if it was the income of an association of persons.**

It was further held by the High Court that as per proviso to section 164(2), it is, *inter alia*, laid down that in cases where the whole or part of the relevant income is not exempt by virtue of section 13(1)(d), tax shall be charged on the relevant income or part of the relevant income at the maximum marginal rate. The phrase “*relevant income or part of relevant income*” is required to be read in contradistinction to the phrase “*whole income*” under section 161(1A). This is only by way of comparison. Under section 161(1A) which begins with a *non-obstante* clause, it is provided that where any income in respect of which a person is liable as a representative assessee consists of profits of business, then tax shall be charged on the whole of the income, in respect of which such person is so liable at the maximum marginal rate. Therefore, reading the aforesaid two phrases show that the Legislature has clearly indicated its mind in the proviso to section 164(2), when it categorically refers to forfeiture of exemption for breach of section 13(1)(d), resulting in levy of maximum marginal rate of tax **only to that part of income, which has forfeited exemption. It does not refer to the entire income being subjected to maximum marginal rate of tax.** This interpretation is also supported by Circular No.387, dt.8.7.1984 [152 ITR (St)1]. It was also held that in law, there is a vital difference between eligibility for exemption and withdrawal of exemption / forfeiture of

exemption for contravention of the provisions of law. These two concepts are different. They have different consequences.

In the circumstances, it was held that there was merit in the contention of the assessee that in the present case, the maximum marginal rate of tax would apply only to the dividend income from shares in Mafatlal Industries Ltd and not to the entire income.

Accordingly, the aforesaid question was answered in the negative, that is, in favour of the assessee and against the Department.

It is, therefore, clearly established that the Bombay High Court approved the judgement of the Tribunal to the effect that non-fulfilment of condition of investment prescribed under section 11(5) of the Act, could not deprive the trust of the exemption of its other income, which had been granted to it in the earlier years. **In other words, it is clearly established that violation of section 13(1)(d) does not tantamount to denial of exemption under section 11 to the total income of the assessee.**

3. *Jamsetji Tata Trust Vs JDIT (E) [2014] 101 DTR (Trib) 305 (Mum)*

It was, *inter alia*, held in this case that violation of section 13(1)(d) and section 13(2)(h) deprives exemption only to the income from investments not permitted under section 11(5) and not to the entire income of the trust, if the other income of the trust, otherwise fulfils the condition for exemption. Therefore, the exemption under section 11 is available to the assessee only in respect of income, to the extent the same is derived in conformity to section 11 and applied during the year for the purposes of the trust.

While reaching the aforesaid conclusion, the Hon. Tribunal has followed the judgement of Bombay High Court, in the case of *DIT(E) Vs Sheth Mafatlal Gagalbhai Foundation Trust [2001] 249 ITR 533 (Bom)*.

It may also be stated here that in the aforesaid judgement, the Tribunal has also followed the earlier judgement of Mumbai Bench of the Tribunal, in the case of *Gurdayal Berlia Charitable Trust Vs ITO [1990] 34 ITD 489 (Bom)*. It was held in this judgement that non-fulfilment of the condition of investment under section 11(5) cannot deprive the trust of exemption of its other income, which has already been granted to it in the earlier years. The non-fulfilment of the condition under section 11(5) would only make a portion of the relevant income as specified under section 164(1), liable to tax. It was further held that in such a

case, the provisions of section 164(2), along with the proviso thereto, would come into operation and only such income would be brought to tax at the maximum marginal rate, which cannot be treated as exempt by virtue of non-fulfilment of the condition of investment under section 11(5) of the Act.

4. *CIT Vs. Red Rose School [2007] 163 Taxman 19 (All.)*

It was, *inter alia*, held in this case that the language used in section 12AA for the registration of a trust, only requires that activities of the trust or the institution must be genuine, which, accordingly, would mean that they are in consonance with the objects of the trust / institution and are not mere camouflage, but are real, pure and sincere and are not against the objects of the trust. The profit earning or **misuse of the income derived by charitable institution from its charitable activities may be a ground for refusing exemption only with respect to that part of the income**, but cannot be taken to be a synonym to the genuineness of the activities of the trust or institution [*Paragraph 34 on pages 32 and 33 of the Report*]

It may, thus, be seen that as per the aforesaid judgement of the Allahabad High Court, the misuse of the income derived by the charitable institution from its charitable activities may be a ground for refusing exemption only with respect to that part of income and not the whole of the income of the trust / institution.

5. *ITO Vs. Virendra Singh Memorial Shiksha Samiti [2009] 18 DTR (Trib.) 502 (Lucknow).*

In this case, allegations were made by the IT Department that the assessee-society was disentitled from getting exemption under section 10(23C), as some benefit was imparted to the founder of the Trust.

It was held that in the first place, there was no evidence that such benefit had been imparted to the founder and secondly, even if it was so, **such instances cannot be imported to deny the exemption under section 10(22) / 10(23C). It was further held that mere disallowance of certain expenses cannot become basis for denying exemption under section 10(22) / 10(23C).**

The aforesaid judgement will be equally applicable to the exemption under section 11 of the Act. Therefore, it is clearly established that even if some benefit has been imparted to the founder of the trust, such instance cannot disentitle the assessee from the benefit of exemption under section 11 of the Act.

6. *Arvind Bhartiya Vidhyalya Samiti Vs. ACIT [2008] 115 TTJ 351 (Jp.)*

It was, *inter alia*, held in this case that even if there was some mis-utilization of the funds / mis-management by the trustees, or minor discrepancies are there, these cannot disentitle the assessee from the exemption under section 10(22) or section 10(23C) of the Act.

The aforesaid judgement will equally apply to the exemption under section 11 of the Act. Therefore even if there is some mis-utilization of the funds /mismanagement by the trustees or there are minor discrepancies, these cannot disentitle the assessee from exemption under section 11 of the Act.

7. *Dy.CIT Vs. Cosmopolitan Education Society [2000] 244 ITR 494 (Raj.)*

In this case, allegations were made against the society that there was mis-utilization or mis-management of the income / funds of the Trust and accordingly, the exemption under section 10(22) of the Act was denied to the assessee.

It was, *inter alia*, held that if there was any mis-utilization or mis-management of the income / funds of the society, action could be taken against the members of the society and the benefit under section 10(22) could not be denied to the society.

It was also held in this case that in view of the judgement of the Supreme Court, in the case of *Aditnar Educational Institution Vs Addl.CIT [1997] 224 ITR 310 (SC)*, an overall view is to be taken without being hyper technical in granting exemption under section 10(22) of the Act.

The aforesaid judgement will equally apply to the exemption under section 11 of the Act. Therefore, if there is some mis-utilization or mis-management of the income / funds, the exemption under section 11 of the Act, cannot be denied to the assessee Trust.

In view of the aforesaid legal precedents, it is clearly established that only the relevant income falling within the mischief of section 13(1)(c) / 13(1)(d) will lose the benefit of exemption under section 11 of the Act and the balance of the total income of the trust will remain eligible for the benefit of exemption under section 11 of the Act. In other words, violation of section 13(1)(c) / 13(1)(d) cannot lead to denial of exemption under section 11 of the Act, to the total income of the trust.

V. In the present context, it is also significant to note that burden of proof lies on the Revenue to prove that section 13 applies in a case.

In the present context, it is also significant to note that burden of proof lies on the Revenue to prove that the provisions of section 13 apply in a case.

Section 13 starts with a *non-obstante* clause and hence by virtue of the said provisions, exception to the exemption provided by section 11, is carved out and an assessee is denied the benefit of exemption under section 11 of the Act, in a case where there is violation of the provisions of section 13 of the Act. It is also relevant to state here that a person who makes a positive statement is required to establish the same. It is not for the person against whom the averment is made to establish negatively that the state of affairs averred by the other person does not exist. Therefore, the exception has to be stated and established by the Revenue. In other words, burden of proof lies on the Revenue.

In support of the aforesaid stand, reliance is placed on the following legal precedents :

1. *Surat City Gymkhana Vs Dy.CIT [2002] 254 ITR 733 (Guj)*

It was, *inter alia*, held in this case that the provisions of section 13 of the Income-Tax Act, 1961, start with a *non-obstante* clause and hence by virtue of the said provisions exception to the exemption provided by section 11 is carved out and as assessee is denied the exemption under section 11 of the Act, in a case where the income or property of the trust is used or applied or enures for the benefit of any person referred to in section 13(3) of the Act. A person who makes a positive averment is required to establish the same. It is not for the person against whom the averment is made to establish negatively that the state of affairs averred by the other person does not exist. The provisions of section 13 carve out an exception to the applicability of the provision of section 11 of the Act and hence, the exception has to be stated and established by the person who seeks to invoke and apply the exception.

2. *CIT Vs Kamala Town Trust [2005] 279 ITR 89 (All)*

It was, *inter alia*, held in this case that section 13 of the Act, carves out an exception to the general exemption granted under sections 11 and 12 of the Act, to the income derived by a trust / charitable institution. The onus lies on the Revenue to bring on record cogent material / evidence to establish that the trust / charitable institution is hit by the provisions of section 13.

In the light of the aforesaid legal precedents, it is clearly established that for the application of the provisions of section 13 of the Act, it is not sufficient on the part of the Assessing Officer (AO) to

simply raise a doubt about the intended purpose of an expenditure incurred by the trust. The AO will have to prove to the hilt, on the basis of positive evidence brought on record, that the trust has committed a violation of the provisions of section 13 of the Act. If the AO is not able to discharge the burden of proof, which lies on him, then he cannot deny the benefit of exemption under section 11 to the trust, on the basis of alleged violation of section 13 of the Act.

VI. Besides, regarding the interpretation of incentive provision like section 11, the approach of the IT Department should be liberal, purposive and broad.

In the present context, it has also to be understood that section 11 is an incentive provision, granting tax benefit to charitable and / or educational institutions. Besides, section 11 is also a provision beneficial to the assessee and a beneficial provision is also to be construed liberally and in favour of the assessee.

In this context, the following rules of interpretation are relevant.

1. Incentive provision is to be liberally construed

It is a well settled position in law that an incentive provision should be liberally construed. For this purpose, reliance may be placed on the following legal precedents.

(i) *P.R. Prabhakar Vs CIT [2006] 284 ITR 548 (SC)*

It was, *inter alia*, held in this case that although the exemption provisions should be construed strictly as regards the applicability thereof to the case of the assessee; but once it is found that the exemption is applicable, the provisions are required to be interpreted liberally.

(ii) *Bajaj Tempo Ltd. Vs CIT [1992] 196 ITR 188 (SC)*

It was, *inter alia*, held in this case that a provision in a taxing statute granting incentives has to be interpreted liberally and the restriction on it too, has to be construed so as to advance the objective of the provision and not to frustrate it.

From the aforesaid legal precedents laid down by the Apex Court it is clearly established that an incentive provision like section 11 should be construed liberally, so as to advance the objective of the provision.

2. Purposive construction - Intention

A purposive approach for interpreting the act is necessary. The Courts must look to the object, which the statute seeks to achieve while interpreting any of the provisions of the Act. For this purpose, reliance may be placed on the following judgements :

(i) *Mysore Minerals Ltd. Vs CIT [1999] 239 ITR 775 (SC)*

It was, *inter alia*, held in this case that the provision should be so interpreted and the words used therein should be assigned such meaning as would enable the assessee to secure the benefit intended to be given by the Legislature to the assessee.

It was also held that where there are two possible interpretations of a taxing provision, the one which is favourable to the assessee should be preferred.

(ii) *CIT Vs Rajesh Kumar Jalan [2006] 286 ITR 274 (Gauhati)*

It was, *inter alia*, held in this case that while construing a beneficial enactment, the view that advances the object of the beneficial enactment and serves its purpose, must be preferred to that which obstructs the objects and paralyses the purpose of the beneficial enactment.

For the above proposition, reliance may also be placed on the following legal precedents.

(a) *S. Gopal Reddy Vs State of Andhra Pradesh JT 1996 (6) SC 268*

(b) *K.P. Varghese Vs ITO [1981] 131 ITR 597 (SC)*

(c) *Indian Hotel Co. Ltd. Vs ITO [2000] 245 ITR 538 (SC)*

From the aforesaid legal precedents, it is clear that the provisions of a taxing statute have to be construed in a manner that the objective / purpose of the enactment is really achieved.

3. A beneficial provision has to be interpreted liberally and in favour of the assessee

As per the judgement in the case of *CIT Vs Gujarat Aluminium Extrusions Pvt. Ltd. [2003] 263 ITR 453 (Guj)*, it is settled legal position that provision for exemption or relief should be construed liberally and in favour of the assessee.

Similar is the view taken in the case of *A.S. Mani Vs Union of India [2003] 264 ITR 5 (Karn)*

4. Ambiguity is to be resolved in tax-payer's favour

The Supreme Court has held that ambiguity in interpretation has to be resolved in favour of the tax-payer. This was held by the Apex Court in the case of *CIT Vs Kulu Valley Transport*

Co. Pvt. Ltd. [1970] 77 ITR 518 (SC) Besides, the view that the benefit of doubt as to interpretation of law should go to the tax-payer is now well established, as held in the following cases.

(a) *CIT Vs Madhav Prasad Jatia [1976] 105 ITR 179 (SC)*

(b) *CIT Vs Vegetable Products Ltd. [1973] 88 ITR 192 (SC)*

(c) *CIT Vs Podar Cement Pvt. Ltd. [1997] 226 ITR 625 (SC)*

5. In case of two possible views, a view beneficial to the assessee is to be preferred

In case of two possible views, a view favourable to the assessee is to be preferred. The aforesaid proposition is supported by the following legal precedents :

(i) *Manish Maheshwari Vs CIT [2007] 289 ITR 341 (SC); and*

(ii) *Pradip J. Mehta Vs CIT [2008] 300 ITR 231 (SC)*

From the aforesaid principles of interpretation of taxing statutes, as laid down by the Apex Court and the High Courts, it is evident that an incentive provision should be liberally interpreted in a manner that the purpose and objective of the enactment are achieved. Besides, a beneficial provision is also to be interpreted liberally and in favour of the assessee. In addition, in case of an ambiguity or two possible views also, a view beneficial or favourable to the assessee is to be preferred.

Besides, in the light of the aforesaid legal precedents the restriction placed by the provisions of section 13, on the benefit available under section 11, should be so interpreted as to grant the benefit of section 11 to the trust and not to deprive the trust of the same.

VII. Conclusion

In the light of the discussion brought out in the preceding paragraphs, the following conclusions are clearly established :

1. As per provisions of section 13(1)(d), it is only the income from such investment or deposit which has been made in violation of section 11(5) of the Act, that is liable to be taxed and violation under section 13(1)(d) does not result in the denial of exemption under section 11 to the total income of the trust.
2. Similarly, as per the provisions of section 13(1)(c), it is only the income or value of the property misused by the trustee that is liable to be taxed and violation under section 13(1)(c) will not result in the denial of exemption under section 11 to the total income of the trust.

3. As regards the provisions of section 13(2), the same being an extension of the provisions of section 13(1)(c) / 13(1)(d), the violations there under will be dealt with on similar lines as the violations under section 13(1)(c) / 13(1)(d) of the Act.
4. The burden of proof lies on the Revenue to prove that the trust has committed any violation of the provisions of section 13 of the Act.
5. Besides, in the light of the legal precedents referred to in the preceding paragraph (V), the restriction placed by the provisions of section 13 on the benefit available under section 11 should be so interpreted, as to grant the benefit of section 11 to the trust and not to deprive the trust of the same.

In the light of the aforesaid reasons, it is only the relevant income falling within the mischief of section 13(1)(c) / 13(1)(d), which is liable to be taxed and violation of the provisions of section 13(1)(c) / 13(1)(d) will not result in denial of exemption under section 11 to the total income of the trust. In other words, the balance of the total income of the trust, will remain eligible for the benefit of exemption under section 11 of the Act.

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