

(2002) 11 AHC CK 0128

Allahabad High Court

Case No: IT Appeal No's. 3 to 6 of 2000

U.P. Forest Corporation

APPELLANT

Vs

Deputy Commissioner of Income
Tax

RESPONDENT

Date of Decision: Nov. 26, 2002

Acts Referred:

- Income Tax Act, 1961 - Section 11(1), 11(2), 11(5), 2(15)

Citation: (2003) 183 CTR 191

Hon'ble Judges: Sudhir Narain, J; M.A. Khan, J

Bench: Division Bench

Advocate: R.K. Srivastava and S.P. Gupta, for the Appellant; S.C. Misra and Pradeep Agarwal, for the Respondent

Final Decision: Allowed

Judgement

Sudhir Narain, J.

The basic issue in the consolidated appeals is whether the income of the appellant is wholly for charitable purpose as defined u/s 2(15) of the IT Act, 1961 (hereinafter referred to as "the Act").

2. The U.P. Forest Corporation, the appellant, was constituted by notification issued u/s 3 of the U.P. Forest Corporation Act, 1974. The assessment proceedings were taken against it. The appellant claimed exemption on the ground that it is a local authority and was liable for exemption u/s 10(20) of the Act. The AO rejected the claim. The respondents then filed appeal and the CIT(A), following the decision of the High Court in Writ Petn. No. 1568 of 1977 for the asst. yr. 1976-77, held that the appellant was a local authority and as such was exempt from tax. The Tribunal, on appeal, set aside this order on the ground that the appellant was not a local authority. The appellant challenged these orders by filing writ petition in the High Court. The High Court allowed the writ petition on 19th May, 1988, on two

grounds--firstly, that the appellant is a local authority and secondly, it was entitled to exemption u/s 11(1)(a) of the Act. The respondents preferred appeals before the apex Court. The appeals were allowed holding that the appellant is not a local authority within the meaning of Section 10(20) of the Act. As regards the exemption claimed under the provisions of Section 11(1)(a) of the Act the assessing authority was directed to consider such claim of the respondent. The AO took the view that the predominant object of the appellant is commercial and, therefore, its income cannot be treated as for charitable purpose within the meaning of Section 2(15) of the Act. The view taken by the AO has been affirmed by the CIT(A) and the Tribunal. These appeals are directed against these orders.

3. Section 11(1)(a) of the Act reads as under :

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

4. The expression "charitable purpose" has been defined u/s 2(15) of the Act reads as under :

"(15) "Charitable purpose" includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility,"

5. The expression "property held in trust" includes business undertaking as provided u/s 11(4) of the Act.

6. Sri S.P. Gupta, learned senior counsel for the appellant, submitted that the object for which the appellant has been constituted under the provisions of U.P. Forest Corporation Act, 1974 (in short 1974 Act) is for general public utility and, therefore, the appellant is entitled to exemption as contemplated u/s 11(1)(a) of the Act.

7. It is next to be examined as to what are the objects of the appellant-corporation. The preamble of 1974 Act, reads as under :

"An Act to provide for the establishment of a corporation for better preservation, supervision and development of forests and better exploitation of forest produce within the state and for matters connected therewith."

8. The Supreme Court in *Orient Paper Industries Ltd. v. State of Orissa* 1991 Suppl. (1) SCC 81 , while considering the objects of Orissa Forest Act, 1972 and Act No. 22 of 1981, observed that legislative object sought to be achieved can be gathered from the preamble of the Act as well as from the Statement of Objects and Reasons. In the [The State of Karnataka and Another Vs. Shri Ranganatha Reddy and Another](#) , while considering the meaning of public purpose in respect of law providing for acquisition of property it was observed as under :

"The intention of the legislature has to be gathered mainly from the Statement of Objects and Reasons of the Act and its preamble"

There cannot be any dispute that preservation, supervision and development of forest are of public utility. Art. 48A of the Constitution provides that the state shall hand over to protect and improve the environment and to safeguard the forest and wild life of the country. Similarly Art. 51A(g) of the Constitution says: It shall be duty of every citizen of India to protect and improve the natural environment including the forest lakes, rivers and wild life and to have compassion for living creatures. The importance and benefit of forest to mankind has been emphasized by various decisions of the Supreme Court. In [T.N. Godavarman Thirumulkpad Vs. Union of India and others](#), the Supreme Court, considering the significance of protection of conservation of forest throughout the country, gave directions to Central Government and the State Governments, referring to the provisions of Forest Conservation Act, 1980. It was observed that the Act was enacted with a view to check deforestation which ultimately results in ecological balance and the provisions were made for the conservation of forests and for matters connected therewith and the direction was that they must be applied to all forests irrespective of the nature of ownership and classification thereof. [M.C. Mehta Vs. Kamal Nath and Others](#), the apex Court applied "doctrine of public trust" in relation to protection of natural resources.

9. The preservation, supervision and development of forest are of general public utility. It does not involve any commercial activity but exploitation of forest produce involves commercial activity. The preservation means the forests are existing and they should not be spoiled by fire, etc. If the trees are dried they may be cut and thereafter new trees be planted in their place. Similarly, supervision required that nobody should cut the trees or damage the forest in any manner. The development of the forest means planting of trees which may develop the forest. On the other hand exploitation of forest produce means to extract forest produce from the trees or other vegetation within the forest, to cut the old trees and sell them in the market. The exploitation thus involves the commercial activities.

10. The mere fact that the commercial activity is done and certain profit is gained but ultimately if such profit is invested or utilised for the purpose of general public utility, then it can be treated for charitable purposes as defined u/s 2(15) of the Act but if it is not utilised for that purpose, then it cannot be treated that the income was held for charitable purpose. This will depend upon the application of fund. Section 11(1)(a) of the Act provides that the income derived from the property held in trust wholly for charitable or religious purpose will be exempt to the extent it is applied to such purposes. This clearly suggests that the income which has been spent on preservation, supervision and development of forest will be of general public utility though the expenses so incurred were from the income derived from exploitation of forest produce.

11. The functions and powers of the Corporation have been enumerated u/s 14 of the 1974 Act which reads as under :

"Subject to the provisions of this Act, and to any general or special directions of the State Government, the functions of the Corporation shall be the following, namely :

(a) to undertake removal and disposal of trees and exploitation of forest resources entrusted to it by the State Government;

(b) to prepare projects relating to forestry within the state;

(c) to undertake research programmes relating to forests and forest products and render technical advice to State Government on matters relating to forestry;

(d) to manage, maintain and develop such forests as are transferred or entrusted to it by the State Government;

(e) to perform such functions as the State Government may, from time to time, required."

12. Section 17 provides for utilization of fund of the Corporation. Sub-section (2) of Section 17 provides that the fund shall be applied towards meeting expenses incurred by the Corporation in the discharge of its function under this Act and for no other purpose.

13. The meaning and scope of words "advancement of any other object of general public utility" came up for consideration before the Privy Council, Supreme Court and High Courts. In [Commissioner of Income Tax, Madras Vs. Andhra Chamber of Commerce](#), the question was whether the rent received from the property by the Andhra Chamber of Commerce was exempt from Income Tax u/s 4(3)(i) of Indian IT Act, 1922. The Supreme Court held that the object of the Chamber of Commerce was advancement of promotion of trade, commerce and industries leading to economic prosperity ensures for the benefit of entire community and such an object shall be treated of general public utility. The definition of "charitable purpose" was inclusive and not exhaustive. It observed :

"... Advancement or promotion of trade, commerce and industry leading to economic prosperity enures for the benefit of entire community. That prosperity would be shared also by those who engaged in trade, commerce and industry, but on that account the purpose is not rendered any the less an object of general public utility...."

It was further clarified with this observation ;

"... To serve as charitable purpose, it was not necessary that the object should be to benefit the whole of mankind or even all persons living in a particular country or province. It was sufficient if the intention was to benefit a section of the public as distinguished from specified individuals.. .."

14. Following the principles enumerated in Andhra Chamber of Commerce case (supra), the income of Hyderabad Stock Exchange Ltd. was held for charitable purpose in [HYDERABAD STOCK EXCHANGE LTD. Vs. COMMISSIONER OF INCOME TAX, A. P.,](#) , on the ground that the aims and objects of assessee, the Stock Exchange, were not only to advance the interests of brokers and dealers but also to assist, regulate and control the trade in securities, to maintain high standards of commercial honour and integrity, to promote and inculcate honourable practices, discourage and suppress malpractice, to settle disputes and decide all questions of usage, custom or courtesy in the conduct of trade and business. The profits were not to be distributed between the members but were to be utilised for the promotion of the objects of the Stock Exchange, Similar view was expressed in [Commissioner Of Income Tax, Madras Vs. Madras Stock Exchange Ltd. And Others.,](#)

15. In [Commissioner of Income Tax, Bombay Vs. Bar Council of Maharashtra,](#) , where the Bar Council of Maharashtra claimed exemption u/s 11(1)(a) of the Act, 1961, on the ground that the income of the Bar Council of Maharashtra derived from interest was for advancement of an object of general public utility within the meaning of Section 2(15) of the IT Act, 1961. It was accepted and was observed as under :

"... In other words, the dominant purpose of a State Bar Council as reflected by the various obligatory functions is to ensure quality service of competent lawyers to the litigating public, to spread legal literacy, promote law reforms and provide legal assistance to the poor while the benefit accruing to the lawyer members is incidental...."

16. The scope of exemption u/s 11(1)(a) of the Act was further clarified in [Additional Commissioner of Income Tax, Gujarat Vs. Surat Art Silk Cloth Manufacturers Association,](#) . The facts were that Surat Art Silk Cloth Manufacturers Association was incorporated under the Companies Act, 1913. It was formed with an object to promote commerce and trade in art silk yarn, raw silk, cotton yarn, art silk cloth, silk cloth, cotton cloth and activities connected therewith. It claimed exemption u/s 11(1)(a) of the Act of its income on the ground that its object was for advancement of general public utility and not for profit. The Supreme Court laid down certain important principles in this case--(1) that the dominant purpose is to be examined, and (2) the mere fact that it involves an activity of profit does not deprive it from claiming the exemption u/s 11(1)(a) of the Act, The observations were as under :

"... The law is well settled that if there are several objects of a trust or institution, some of which are charitable and some non-charitable and trustees or the managers in their discretion are to apply the income or property to any of those objects, the trust or institution would not be liable to be regarded as charitable and no part of its income would be exempt from tax. In other words, where the main or primary objects are distributive, each and every one of the objects must be charitable in order that the trust or institution might be upheld as a valid charity:

vide Mohd. Ibrahim v. CIT (1930) 57 IA 260 and [East India Industries \(Madras\) Private Limited Vs. Commissioner of Income Tax, Madras](#), . But if the primary or dominant purpose of a trust or institution is charitable, another object which by itself may not be charitable but which is merely ancillary or incidental to the primary or dominant purpose would not prevent the trust or institution from being a valid charity : vide [Commissioner of Income Tax, Madras Vs. Andhra Chamber of Commerce](#), ...".

"... 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. The decisions of the Kerala and Andhra Pradesh High Courts in [Commissioner of Income Tax Vs. Cochin Chamber of Commerce and Industry](#), and [Andhra Pradesh State Road Transport Corporation Vs. Commissioner of Income Tax](#), , in our opinion, lay down the correct interpretation of the last ten words in Section 2, Clause (15). The true meaning of these last ten words is that when the purpose of a trust or institution "is the advancement of an object of general public utility, it is that object of general public utility and not its accomplishment or carrying out which must not involve the carrying on of any activity for profit."

17. The contrary view taken in [Indian Chamber of Commerce Vs. Commissioner of Income Tax , West Bengal II, Calcutta](#), was overruled observing that :

"What these last concluding words require is not a trust or institution whose purpose is advancement of an object of general public utility should not carry on any activity for profit at all but the purpose of the trust or institution should not involve the carrying on any activity for profit, the requirement of the definition would be met and it is immaterial how the monies for achieving or implementing such purpose are found, whether by carrying on an activity for profit or not."

18. When statutory Corporation shall be entitled to exemption u/s 11(1)(a) of the Act came for consideration in [Commissioner of Income Tax, A.P. Vs. Andhra Pradesh State Road Transport Corporation](#), . where the Road Transport Corporation which was established by a notification issued under s, 3 of the Road Transport Corporation Act, 1950 by the State of Andhra Pradesh claimed exemption for Income Tax u/s 11(1)(a) of the Act. Section 3 of the said Act enumerated the objects for which the Road Transport Corporation was established, namely (a) offering advantages to the public, trade and industry by the development of road transport; (b) coordinating any form of road transport with any other form of transport; and (c) extending and improving the facilities for road transport in any area and of providing an efficient and economical system of road transport service therein, it was held that activity of the Transport Corporation was not carried on with the object of making profit. The Court relied upon Section 30 of the said Act which provided that the balance income left after utilization for the purpose set out

therein was to be made over to the State Government for the purpose of road development. The Supreme Court upheld the contention that where an activity is carried on with the object of general public utility it would not cease to be charitable in character even though its activity was carried on commercial lines with the object of earning profit. The Court referred to Section 22 of the said Act which provided that in carrying on undertaking by the Transport Corporation it shall act on business principles. The earning has to be made on the business principles otherwise there will be no profit and in absence of profit the amount cannot be invested for the development of road, etc, It was observed ;

". . . No activity can be carried on efficiently, properly, adequately and economically unless it is carried on business principles. If an activity is carried on business principles, it would usually result in profit, but, as pointed out by this Court in Swat Art Silk Cloth Mfrs. Association's case (supra), it is not possible so to carry on a charitable activity in such a way that the expenditure balance the income and there is no resultant profit, for, to achieve this, would not only be difficult of practical realisation but would reflect unsound principles of management. ..."

19. Shri Pradeep Agarwal, learned counsel for the respondent has placed reliance on [Bihar State Forest Development Corporation Vs. Commissioner of Income Tax](#) wherein the case of Andhra Pradesh State Road Transport Corporation (supra) was distinguished. The fact therein was that Bihar State Forest Development Corporation was registered as a Government company within the meaning of Section 617 of the Companies Act, 1956. One of the objects of its Memorandum of Association was to promote, establish, execute, and operate projects and schemes relating to exploitation of forest and conversion of natural forest areas into artificial plantations of valuable species and to manage forest plantations. The Court recorded a finding that objects of the company may appear to be of general public utility for development of forestry but then there were other objects as well, which made the assessee a commercial organisation with no restriction as to how its income would be utilised. The observation is quoted as under :

"Again that is not the case before us. Thus, the aforesaid two decisions are clearly distinguishable and do not apply to the facts of the present case. The objects with which the assessee was incorporated as a company may appear to be of general public utility for development of forestry, but then there were other objects as well which make the assessee a commercial organisation with no restriction as to how its income would be utilised. Thus, considering the principles set out in the aforesaid decision of the Supreme Court we find no difficulty in answering the first question in the affirmative, in favour of the Revenue and against the assessee."

20. Sri S.P. Gupta, learned senior counsel for the appellant, has drawn distinction between the object of a corporation and its functions and powers and has placed reliance upon the decision in *Thiagarajar Charities v. Addl. CIT and Anr.* : [1997]225ITR1010(SC) . The contention of the assessee in this case was that though

it carries on business of purchase and sale of cotton yarn and cloth and other fabrics both wholesale and retail and if income derived is spent on the objects of the trust, namely, to establish, maintain schools, colleges, workshops, industrial, technical and other institutes and rural constructions and the income spent on it should be exempt u/s 11(1)(a) of the Act. The Supreme Court held that there is a distinction between the objects of a company and powers of the company to be exercised in effecting the objects. The passage from the judgment of Lord Wrenbury was quoted which reads as under :

"The objects of the company and the powers of the company to be exercised in effecting the objects are different things. Powers are not required to be, and ought not to be, specified in the memorandum. The Act intended that the company, if it be a trading company, should by its memorandum define the trade, not that it should specify the various acts which it should be within the power of the company to do in carrying on the trade. The Third Schedule of the Act contains model forms of Memorandum of Association. These ought to be followed. Section 118, Sub-section (1), enacts that those forms "or forms as near thereto as circumstances admit" shall be used in all matters to which those forms refer."

21. The assessee was given exemption of tax only insofar as the amount spent on charities which will be clear from the following passage :

"It appears from the affidavit filed by the appellant trust, which is available at p. 142 of the paper book, that an aggregate sum of Rs. 16,48,030 was spent for charitable purposes during the period from 4th June, 1962, to 31st May, 1967. The purposes are aid to the various colleges, orphanages, relief to the poor and different categories or types of education. It also appears that in one of the assessment years, the amount so applied is much more than the total income. The facts available in the records go to show that the profits are amounts earned in the business fed the charitable purposes specified in the trust deed. In other words, the amounts earned had been essentially spent on charity. There can be no doubt that profit-making was not the real object of the trust."

22. The following propositions can be culled out from the above decision :

(a) Even if the object or the purpose may not be regarded as charitable in its popular significance as not tending to give relief to the poor or for advancement of education or medical relief, it would still be included in the expression "charitable purpose", if it advances an object of general public utility.

(b) An object beneficial to a section of public is an object of public utility as distinguished from specified individuals.

(c) The expression of object of general public utility would prima facie include all objects which promote the welfare of general public.

(d) If the main predominant object is of public utility the mere fact that income is also generated by that activity will not nullify or neglect the charitable purpose.

(e) For application of income for the purpose of charity the person or institution can engage itself in commercial activity but with a predominant object of applying it for charitable purpose.

Applying the above principles we find that the income derived from exploitation of forest is commercial activity. The income, however, spent on preservation, supervision and development of forest will be treated for the general public utility and shall be exempt u/s 11(1)(a) of the Act provided other conditions provided under the said provision are satisfied. The income which is not spent for such activities will not be exempt under this provision. The view of the Tribunal that as the income is derived from the exploitation of forest by the appellant and, therefore, its income shall not be exempt u/s 11(1)(a) is erroneous.

23. As the Tribunal has not applied this principle, we remit the matter back to the Tribunal to decide the appeals afresh in accordance with the observations made above. It will examine the total income of the appellant for the assessment years in question and thereafter it will take into consideration the income applied by the appellant specifically for the purpose of preservation, supervision and development of forest on the principle laid down in *Thiagarajar Charities*" case (supra).

24. The next question is regarding exemption of any income accumulated or set apart for purposes of charity to the extent to which the income so accumulated or set apart is not in excess of 25 per cent of the income derived by the appellant as provided in Clause (a) of Sub-section (1) of Section 11 of the IT Act. In order to enjoy exemption to the full extent, at least 75 per cent of the trust income has to be utilised in the accounting year itself to charity purpose. "Secondly the benefit shall be given only if the condition mentioned in Sub-section (2) of Section 11 of the Act is complied with, namely, the person claiming exemption by notice in writing given to the AO in the prescribed manner indicates the purpose for which the income is being accumulated or set apart and the period for which the income is to be accumulated or set apart, which in no case exceeds 75 per cent and thirdly the money so accumulated or set apart is invested or deposited in the form and manner specified in Sub-section (5) of Section 11 of the Act. The appellant has not shown that it has complied with the condition referred to in Sub-section (2) of Section 11 of the Act. In case the income is derived from commercial activities and the income is accumulated by such trust it cannot be held that the income was accumulated only for charitable purpose. The appellant is thus not entitled to exemption of any amount accumulated by it.

25. The appellant has further raised a question as to whether the Tribunal was right in remanding the matter in respect of interest under Sections 215 217 139(8) and 234A 234B 234C and 220(2) of the IT Act, 1961 to the AO. As the question raised

involves question of fact and we do not find that the view taken by the Tribunal in remanding the matter of interest is erroneous.

26. In view of the above discussion we allow the appeal and remand the matter to the Tribunal to consider the matter afresh keeping in view the above observations.