
American Hotel and Lodging Educational Institute (Earlier known as Educational Institute of American Hotel and Motel Association) Vs The Central Board of Direct Taxes Ministry of Finance, Government of India, The Director of Income Tax, The Assistant Director of Income Tax and The Union of India (UOI)

Writ Petition No. 1152 of 2010

Court: Bombay High Court

Date of Decision: June 30, 2010

Acts Referred:

Constitution of India, 1950 " Article 226#Finance (No. 2) Act, 1998 " Section 10#Income Tax Act, 1961 " Section 10, 10(22), 10(23C), 12AA

Citation: (2010) 235 CTR 223 : (2010) 329 ITR 16 : (2010) 192 TAXMAN 275

Hon'ble Judges: J.P. Devadhar, J; D.Y. Chandrachud, J

Bench: Division Bench

Advocate: J.D. Mistri, R. Murlidhar and P.C. Tripathi, for the Appellant; Suresh Kumar, for the Respondent

Judgement

D.Y. Chandrachud, J.

Rule. With the consent of Counsel (i) rule is made returnable forthwith; and (ii) the petition is taken up for hearing

and final disposal.

2. The petitioner claims to be a non-profit organization, established in the United States, and has a branch in India through which it carries out

educational activities. The principal challenge in these proceedings is to an order dated 3 November 2009 issued by the Central Board of Direct

Taxes (CBDT) to the extent to which it imposes a condition that the petitioner must "apply 75% of its accounting income for educational purposes

in India". Alternatively, there is a plea that the condition should be applied prospectively and that the petitioner be granted a reasonable period for

compliance. There is an ancillary challenge in these proceedings to an order dated 22 December 2009 issued by the Director of Income Tax

(International Taxation), the second respondent, directing the petitioner to furnish security to cover the demand of tax for assessment years 1999-

2000 to 2006-2007. The petitioner has sought a stay on the recovery of the outstanding demand for these assessment years. For assessment years

1999-2000 to 2001-2002 approval has been granted to the petitioner u/s 10(23C)(vi) of the Income Tax Act, 1961 by the Central Board of

Direct Taxes subject to the condition noted earlier. For assessment years 2002-2003 to 2006-2007, orders have still not been passed by the

Central Board of Direct Taxes or by the prescribed authority. The grievance of the petitioner is that the inaction on the part of the respondents is in

breach of the principles laid down by the Supreme Court in a decision rendered on 9 May 2008 in American Hotel and Lodging Association

Educational Institute Vs. Central Board of Direct Taxes and Others, . This decision was rendered on an appeal of the petitioner against a judgment

of the Delhi High Court.

3. The petitioner entered into a Memorandum of Understanding (MoU) on 27 May 1993 with the National Council for Hotel Management and

Catering Technology, which is an apex Indian body overseeing education in hotel management and catering. Pursuant thereto, the petitioner is

required to offer its courses and expertise in order to improve the quality of hospitality education and training in India. As part of its obligations

under the MoU, the petitioner provides a curriculum for hospitality education programs, course materials, a faculty development program,

certification and registration and an accreditation system to permit the National Council to recognize proprietary schools.

4. The petitioner filed an application on 27 June 1995 with the Authority for Advance Rulings, constituted under Chapter IX-B of the Income Tax

Act, 1961, for seeking a clarification on its tax status. By its ruling of 14 February 1996, the Authority came to the conclusion that the petitioner

fulfills the conditions for the grant of an exemption u/s 10(22) of the Act, as it then stood.

5. Section 10(22) was substituted by Section 10(23C)(vi) by Finance Act (No. 2), 1998 with effect from 1 April 1999. Section 10 provides that

in computing the total income of a previous year of any person, any income falling within any of the clauses of the Section shall not be included.

Sub-clause (vi) of Clause (23C) refers to any income received by any person on behalf of any university or other educational institution existing

solely for educational purposes and not for the purposes of profit, other than those mentioned in sub-clause (iiiab) and (iiiad) and which may be

approved by the prescribed authority. Under the First proviso, an application has to be made to the prescribed authority for the grant or

continuance of the exemption. By the Second proviso, the prescribed authority is empowered to call for documents including audited annual

accounts or information in order to satisfy itself about the genuineness of the activities of the institution. The Third proviso makes provisions inter

alia for the accumulation of the income. A provision has been made by the thirteenth proviso for the withdrawal of approval inter alia where the

activities of the institution are found not to be genuine or to be carried otherwise than in accordance with the conditions subject to which approval

was granted. As a result of the provisos, several provisions came to be incorporated for regulating the grant of approvals and for monitoring

compliance of the conditions subject to which approvals have been granted.

6. In terms of the newly substituted provision, the petitioner made an application to the First respondent on 7 April 1999 for a block of assessment

years, 1999-2000 to 2001-2002. Similar applications were made for two blocks of assessment years - 2002-2003 to 2004-2005 and

assessment years 2005-2006 and 2007-2008 on 16 July 2002 and 9 May 2005. The application for assessment years 1999-2000 to 2001-2002

was rejected by the Central Board of Direct Taxes on 12 October 2004 on the ground that the petitioner was not an educational institution

established in India and that it had a surplus under its balance sheet and profit and loss account for the year ending 31 March 1999.

7. A writ petition under Article 226 was filed by the petitioner, before the Delhi High Court. The petition was dismissed on 24 November 2006. In

an appeal by the petitioner, the Supreme Court delivered judgment in American Hotel and Lodging Association Educational Institute v. Central

Board of Direct Taxes (supra) on 9 May 2008. The Supreme Court set aside the order dated 12 October 2004 and remitted the case back to the

Central Board of Direct Taxes for a fresh consideration in accordance with law. The Supreme Court clarified that the petitioner had fulfilled the

threshold condition of the actual existence of an educational institute u/s 10(23C)(vi) and consequently directed the Board not to reject the

application for approval dated 7 April 1999 on that ground.

8. Since the controversy in the present case arises out of the developments that have taken place after the decision of the Supreme Court, it would

be necessary to make a reference to the salient principles that have been laid down in the judgment. The following principles emerge from the

judgment of the Supreme Court:

(i) The recipient of the income must have the character of an educational institution in India, which must be ascertained from the nature of its

activities. The nature of activities undertaken in India must be considered. If the Indian activity has no co-relation to education, an exemption has to

be denied;

(ii) If after meeting the expenditure, a surplus remains incidentally from the activity carried on by the educational institution, the institution will not

cease to be one which exists solely for educational purposes;

(iii) The location of the University or institution is not relevant and the test is whether education is imparted in India;

(iv) With the insertion of the provisos to Section 10(23C)(vi) an applicant who seeks approval has not only to show that it is an institution which

exists solely for educational purposes but it has to obtain an initial approval from the prescribed authority by making an application as stated in the

first proviso to the Section.

(v) The condition of obtaining approval from the prescribed authority was imposed by Parliament in order to obviate the abuse of the statutory

exemption and a monitoring mechanism has been enacted to check abuse;

(vi) The second proviso lays down the powers and duties of the prescribed authority while vetting an application for approval. The prescribed

authority is empowered to call for documents including annual accounts or information to check the genuineness of the activities of the institution;

(vii) Under the third proviso, the prescribed authority, while judging the genuineness of the activities of the applicant, has to ascertain whether the

applicant applies its income wholly and exclusively for the objects for which it is constituted or established;

(viii) Under the twelfth proviso, the prescribed authority is required to examine cases where an applicant does not apply its income during the year

of receipt and accumulates it but makes payment therefrom to a trust or institution registered u/s 12AA or to any fund or trust or institution or

university or other educational institution;

(ix) Under the thirteenth proviso, a power is given to the prescribed authority to withdraw the approval which has been granted earlier;

(x) There is a difference between stipulation of conditions and compliance of conditions. The threshold conditions are the actual existence of an

educational institution and approval of the prescribed authority. It is only if the condition of existence is fulfilled, that the question of compliance

with the stipulations set out in the provisos would arise. The third proviso contains monitoring conditions such as application and accumulation of

income;

(xi) In order to make the provision workable, the monitoring conditions specified in the third proviso can be stipulated as conditions subject to

which approval is granted by the prescribed authority. The prescribed authority has the power to grant an approval subject to terms and conditions

so long as they are not in conflict with the Act including compliance with the monitoring conditions. While imposing stipulations subject to which

approval is granted, the prescribed authority may insist that a certain percentage of accounting income is utilized / applied for imparting education in

India;

(xii) The prescribed authority may grant approval on such terms and conditions as it deems fit in case where an application is made for initial

approval for the first time. The prescribed authority must give an opportunity to the institute to comply with the monitoring conditions stipulated for

the first time by the third proviso;

(xiii) Cases where the applicant has obtained exemption earlier need not be reopened on the ground that the third proviso has not been complied

with. However, after the grant of approval, if it is brought to the notice of the prescribed authority that the conditions on which approval is granted

are breached or that the circumstances mentioned in the thirteenth proviso exist, the prescribed authority is empowered to withdraw approval;

(xiv) An applicant who is desirous of availing of an exemption u/s 10(23C)(vi) must fulfill the condition that it imparts education in India.

9. On 23 February 2009 an order was passed by the Deputy Director of Income Tax (International Taxation) making a demand for arrears of

Income Tax in the amount of Rs. 10.48 crores for assessment years 2000-2001 to 2006-2007. The grievance of the petitioner is that the demand

for arrears was made without complying with the directions of the Supreme Court, pursuant to which the Central Board of Direct Taxes was

required to consider the application for approval u/s 10(23C)(vi) afresh in accordance with law.

10. The petitioner submitted a representation on 3 March 2009. On 30 March 2009 an order was passed by the Director of Income Tax

(International Taxation) noting that consequent to the decision of the Supreme Court, the Central Board of Direct Taxes was seized of the issue

relating to the grant of exemption to the petitioner. The order was that pending the outcome of the proceedings before the Central Board of Direct

Taxes no action can be taken for recovery. Consequently, the recovery of the outstanding demands was kept in abeyance till the decision of the

Central Board of Direct Taxes. Though the text of the order that was passed by the Director of Income Tax (International Taxation) referred to

assessment years 1999-2000 to 2006-2007, the covering letter addressed to the petitioner on 30 March 2009 made a reference only to

assessment years 1999-2000 to 2001-2002 for which, it was stated, that the demand was kept in abeyance pending the decision of the Central

Board of Direct Taxes. The petitioner by its letter dated 7 April 2009 sought a clarification on this issue.

11. On 19 October 2009, a notice to show-cause was issued to the petitioner to explain as to why the stay that was granted on 30 March 2009

should not be revoked on the ground that the Supreme Court had not stayed the demand. The petitioner by its reply dated 28 October 2009 drew

the attention of the authority to the fact that though over a year had elapsed since the judgment of the Supreme Court, the CBDT had not passed

orders on the application for approval u/s 10(23C)(vi). Proceedings were instituted before this Court under Article 226 of the Constitution. On 4

November 2009 an order was passed by the Director of Income Tax (International Taxation) requiring the petitioner to pay the demand of Rs.

3.87 crores for assessment years 1999-2000 to 2002-2003.

12. In the meantime, on 3 November 2009, the application for grant of approval u/s 10(23C)(vi) was decided. The Central Board of Direct Taxes

granted its approval to the petitioner subject to the condition inter alia that ""the assessee will apply 75 per cent of its accounting income for

educational purposes in India"". The approval is for assessment years 1999-2000, 2000-2001 and 2001-2002.

13. The petition before the Division Bench was thereupon disposed of on 1 December 2009. The Division Bench recorded the statement of the

Revenue that if an application was filed to that effect, the order dated 4 November 2009 would be considered in review. Eventually, an order has

been passed on 22 December 2009 by the Director of Income Tax (International Taxation) calling upon the petitioner to furnish security to cover

the total outstanding demand. One of the submissions that was urged before the authority is that as a matter of fact the petitioner had duly complied

with the condition that 75 per cent of its income should be applied for educational purposes in India. The authority however observed that it would

not be appropriate to examine the issue since the issue as to whether the condition laid down by the Board was fulfilled would have to be decided

by the Assessing Officer.

14. In support of the petition, the Counsel appearing on behalf of the petitioner submitted that: (i) the condition which has been imposed while

granting approval u/s 10(23C)(vi) is impossible of compliance. The condition requires the petitioner to expend at least 75 per cent of its total

income for educational purposes in India for assessment years 1999-2000 to 200 1-2002, which have elapsed. The petitioner had no notice that

such a condition would be imposed and the condition is arbitrary; (ii) The Supreme Court in the course of its judgment has observed that the

prescribed authority must give an opportunity to the applicant - institute to comply with the monitoring conditions which have been stipulated for

the first time by the third proviso. In breach of the directions of the Supreme Court, no such opportunity has been granted; and (iii) Despite the

directions that were issued by the Supreme Court, no order has been passed for assessment years 2002-2003 to 2006-2007. The demand for

taxes in the circumstances is, it is urged, arbitrary.

15. On the other hand Counsel for the Revenue has placed reliance on the affidavit in reply that has been filed in these proceedings and has drawn

the attention of the Court to the fact that the appeals of the assessee against the assessment order for assessment year 1999-2000 are pending

before the Commissioner of Income Tax (Appeals) and for assessment years 2000-2001, 200 1-2002 before the Tribunal. It has also been stated

in the affidavit that in view of the approval granted by the Central Board of Direct Taxes on 3 November 2009, the Assessing Officer would have

to rework the demand for assessment years 1999-2000 to 200 1-2002. Counsel for the revenue however had no justification to advance for the

failure of the prescribed authority to pass an order on the application u/s 10(23C)(vi) for assessment years 2002-2003 to 2006-2007, which

continues to remain pending.

16. The first submission that has been urged on behalf of the petitioner is that while granting its approval, the Central Board of Direct Taxes was

not within jurisdiction in imposing a condition, by its letter dated 3 November 2009, that the petitioner must apply Seventy Five per cent of its total

income for educational purposes in India. The submission is that the condition which has been imposed by the Board would operate for assessment

years 1999-2000 to 2001-2002, which are over. Hence, it was urged that the assessee cannot comply with the condition. In our view, such an

argument is not open to the petitioner in view of the judgment of the Supreme Court, when it decided the appeal filed by the petitioner, on 9 May

2008. The Supreme Court observed that the requirement of obtaining initial approval was introduced by Parliament in Section 10(23C)(vi) in

order to obviate abuse of the exemption provisions. By and as a result of the amendment Section 10(22) stands substituted by Section 10(23C)

(vi). Provisions have been made for scrutiny of applications; for monitoring compliance; and for withdrawal of approval in the event of breach. The

Supreme Court held that the monitoring conditions which have been provided in the third proviso to Section 10(23C)(vi) can be stipulated as

conditions subject to which approval can be granted by the prescribed authority. While advertent specifically to the case of the petitioner, the

Supreme Court observed thus:

...For example, in marginal cases like the present case, where the appellant - institute was given exemption up to the financial year ending March

31, 1998 (assessment year 1998-99) and where an application is made on April 7, 1999, within seven days of the new dispensation coming into

force, the prescribed authority can grant approval subject to such terms and conditions as it deems fit provided they are not in conflict with the

provisions of the 1961 Act (including the above mentioned monitoring conditions). While imposing stipulations subject to which approval is

granted, the prescribed authority may insist on certain percentage of accounting income to be utilized / applied for imparting education in India....

In subsequent observations, the Supreme Court has clarified that the prescribed authority may grant its approval on such terms and conditions as it

deems fit. Where an institute applies for initial approval for the first time, the authority must furnish an opportunity to the institute to comply with the

monitoring conditions which have been stipulated for the first time by the third proviso. In that context, the Supreme Court held that where the

applicant had obtained an exemption earlier, as in this case, the case need not be reopened on the ground that the third proviso has not been

complied with. However, after the grant of approval if it is brought to the notice of the authority that the conditions subject to which the approval

was granted were breached or if the circumstances in the thirteenth proviso exist, the approval which has been granted earlier can be withdrawn by

following due procedure. These observations have been made in the context of monitoring compliance with the conditions subject to which

approval has been granted. As regards the imposition of conditions of approval, the Supreme Court has categorically held that such conditions

could be imposed including a condition that a certain percentage of the accounting income should be utilized or applied for imparting education in

India.

17. Even as a matter of first principle, the imposition of such a condition cannot be faulted. The rationale for the grant of an exemption under the

erstwhile provisions of Section 10(22) and under the amended provision that is now made in Section 10(23C)(vi) is that the institute must impart

education in India. Section 10(23C)(vi) requires that the institution should, to qualify for an exemption, exist solely for educational purposes and

not for the purposes of profit. Imparting education in India is the foundation with reference to which the beneficial provisions of Section 10(23C)

(vi) are enacted. The Central Board of Direct Taxes or the prescribed authority in which the power to grant approval is vested must undoubtedly

have the power to ensure that the object of imparting education in India is duly fulfilled. The requirement that a certain percentage of the accounting

income should be applied or utilized for imparting education in India is consistent with the statutory purpose and is intravires the provisions of the

statute.

18. At the same time, the Supreme Court noted that an conditions. In the present case, a considerable amount of delay has taken place on the part

of the CBDT for reasons which are inexplicable. Even after the decision of the Supreme Court which was rendered on 9 May 2008, the Central

Board of Direct Taxes, or, as the case may be, the prescribed authority took nearly 18 months to pass an order on the application for approval.

Moreover, it is only the application for assessment years 1999-2000 to 2001-2002 that has been disposed of. The application for assessment

years 2002-2003 to 2006-2007 continues to remain pending. Counsel for the Revenue had absolutely no explanation to offer for the delay. The

demands which have been made for the recovery of arrears have been issued with a considerable amount of haste. If, as submitted on behalf of the

petitioner it is entitled to approval u/s 10(23C)(vi) and has complied with the conditions subject to which approval was granted, the basis of the

demands would cease to exist. Whether the conditions subject to which approval was granted have been fulfilled would need to be verified. That is

part of the process of monitoring compliance. This verification has not been done. The pending applications for approval should have been

disposed of expeditiously. This too has not been done.

19. Hence, while we are of the view that the Central Board of Direct Taxes was justified in imposing a condition that a certain proportion (Seventy

Five per cent) of the accounting income should be applied and utilized for educational purposes in India, it is only appropriate and proper that (i)

The contention of the petitioner that it has duly fulfilled the conditions of approval is verified; (ii) An opportunity is furnished to the petitioner, in the

event of a the short fall being found by the Assessing Officer, of a reasonable period for making up the deficit. We propose to pass orders

directing the prescribed authority to dispose of the applications u/s 10(23C)(vi) for the remaining assessment years expeditiously within a

prescribed time schedule. While we uphold the conditions for approval that have been imposed by the Central Board of Direct Taxes for

assessment years 1999-2000 to 2001-2002, we will direct that verification of compliance be made and an opportunity be granted to the

petitioner, upon a determination being made by the Assessing Officer, to bridge the short fall, if any within a reasonable period. Hence, following

order:

i) The prescribed authority is directed to pass orders on the applications for approval made by the petitioner for assessment years 2002-2003 to

2006-2007 expeditiously and in any event within a period of two months from today;

ii) The conditions imposed by the Central Board of Direct Taxes in its order dated 3 November 2009, while granting approval to the petitioner u/s

10(23C)(vi) including the condition that the petitioner must apply Seventy Five per cent of its total income for educational purposes in India are

upheld as valid;

iii) The prescribed authority is directed, in terms of the observations contained in para 33 of the judgment of the Supreme Court dated 9 May

2008 (supra), to furnish to the petitioner an opportunity to comply with the monitoring conditions and to allow a reasonable period to do so in the

event of the Assessing Officer coming to the conclusion that there is any short fall in compliance after considering the expenditure allowable under

the Act;

iv) During the period that may be allowed by the prescribed authority in terms of the directions contained herein above, there shall be a stay on the

recovery of the outstanding demands for assessment years 1999-2000 to 2001-2002 and 2002-2003 to 2006-2007.

20. Rule is made absolute accordingly. The petition is disposed of in terms of this order. There shall be no order as to costs.