IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 26TH DAY OF FEBRUARY 2016

PRESENT

THE HON'BLE MR.JUSTICE JAYANT PATEL

AND

THE HON'BLE MRS.JUSTICE S. SUJATHA

ITA Nos.279 & 280/2010
C/W
ITA No.173/2009

BETWEEN:

M/S. KORAMANGALA CLUB
CA 17, 6TH CROSS, 6TH BLOCK
KORAMANGALA, BANGALORE-560 034
REPRESENTED BY ITS
HON'BLE SECRETARY
MR.C RAJENDRA
AGED ABOUT 58 YEARS
S/O MR.CHINAPPA REDDY
(IN ITA 279 & 280/2010)
MR.G.RAM PRASAD
AGED ABOUT 42 YEARS
SON OF MR.G.VEERARAGHAVAIAH.
(IN ITA 173/2009)

…. APPELLANT
(COMMON IN BOTH THE CASES)

(BY SMT.JINITA CHATTERJEE, ADV FOR
MR.S PARTHASARATHI, ADV)

AND:

THE INCOME-TAX OFFICER
WARD-7(3), KENDRIYA SADAN
KORAMANGALA
BANGALORE-560 034.

... RESPONDENT
(COMMON IN BOTH THE CASES)

(BY SRIYUTHS: E I SANMATHI AND
K V ARAVIND, ADVS)

ITA Nos.279 & 280/2010 ARE FILED UNDER SECTION 260-A OF INCOME TAX ACT 1961, PRAYING TO SET ASIDE THE OREDER PASSED BY THE ITAT BANGALORE IN ITA Nos.1030 & 1031/BANG/2009 DATED 01.04.2010, IN THE INTEREST OF JUSTICE AND EQUITY.

ITA NO.173/2009 IS FILED UNDER SECTION 260-A OF INCOME TAX ACT 1961, PRAYING TO SET ASIDE THE ORDER PASSED BY THE ITAT BANGALORE IN ITA NO.391/BANG/2008, DATED 12.12.2008 CONFIRM THE ORDERS OF THE APPELLATE COMMISSIONER AND ITAT, BANGALORE.

THESE APPEALS HAVING BEEN HEARD AND RESERVED FOR JUDGMENT ON 22ND FEBRUARY 2016, COMING ON FOR PRONOUNCEMENT OF JUDGMENT THIS DAY, S.SUJATHA J., DELIVERED THE FOLLOWING:

COMMON JUDGMENT

These appeals under Section 260-A of the Income-tax Act 1961, (hereinafter referred to as 'the Act' for short) are by the

assessee against the orders passed by the Tribunal, Bengaiuru Bench.

2. The following substantial question of law arises for adjudication before this court:

> *"1. Whether the finding of the Income-tax Appellate Tribunal holding that the provisions of Section 44AB of the income Tax Act, are applicable to the appellant Club, which is a mutual concern, is perverse and arbitrary and contrary to law?*
>
> *2. Whether in the facts and circumstances of the case, the order passed by the Tribunal imposing penalty on the appellant under Section 271B of the Income Tax Act, is perverse and arbitrary having regard to the explanation offered by the assessee?."*

3. The appellant-Club is a registered society, the objectives of which, are as under:

> *"1. To promote sports of all kinds and description.*
>
> *2. To arrange literary and cultural activities including concerts and other entertainments*

3. To establish and maintain a library and reading room.

4. To provide indoor and outdoor games and amusements.

5. To conduct Exhibition, Excursions, Publication of Magazines, etc.,

6. To give scholarships, Free ships, Prizes and Monetary assistance to poor students to help them in their studies and to render financial assistance to run free libraries and free reading rooms.

7. To contribute donations to social service organizations and for socio-economic activity.

8. And generally to do all such other lawful things as are incidental, conducive, or may be necessary in the interest of the society and to promote physical, moral and intellectual development and social and cultural welfare of the Members and their families.

9. To promote and encourage fellowship and "spirit de'cors" amongst the Members and their families."

4. The appellant had failed to obtain the audit report under Section 44AB of the Act, for which proceedings under Section 271B of the Act were initiated by the assessing officer while concluding the assessments for the relevant assessment

years. The appellant offered an explanation that the appellant-club was the mutual concern and was supplying the liquor and beverages only to its members and there was no business carried on by the appellant and accordingly, it was under the bonafide belief that the provisions of Section 44AB of the Act were not applicable to it. Consequently, the appellant did not obtain the audit report at the time of filing of the return of income. The assessing Officer rejected the explanation offered by the appellant and levied the penalty. Aggrieved by the penalty order, the appellant preferred appeals before the Appellate Commissioner, who had upheld the levy of penalty. On further appeal before the ITAT Bangalore by the appellant, the Tribunal dismissed the appeals confirming the levy of penalty. Aggrieved by the said order of the ITAT Bangalore, the appellant is before this Court.

5. We have heard Smt.Jinitha Chatterjee, learned counsel appearing for Sri. S.Parthasarathi for the appellant-assessee and Sri. E.I.Sanmathi along with K.V.Aravind for the respondent-revenue and perused the material on record.

6. The Apex Court in the case of *JOINT COMMERCIAL TAX OFFICER vs. YOUNG MEN'S INDIAN ASSOCIATION [AIR 1970 SC 1212], w*hile considering the case of a club, supplying various refreshments prepared in the club to its members, whether involves a transaction of sale or not has held as under:

> *"The essential question, in the present case, is whether the supply of the various preparations by each club to its members involved a transaction of sale within the meaning of the sale of goods Act 1930. The Sate Legislature being competent to legislate only under Entry 54, List II of the 7th Schedule to the Constitution the expression "sale of goods" bears the same meaning which it has in the aforesaid Act. Thus in spite of the definition contained in Section 2(n) read with Explanation I of the Act if there is no transfer of property from one to another there is no sale which would be exigible to tax. If the club even though a distinct legal entity is only acting as an agent for its members in the matter of, supply of various preparations to them no sale would be involved (1) [1968] 2 S.C.R.421. (2) [1924] 1K.B.390. as the element of transfer would be completely absent. This position has been rightly accepted even in the previous decision of this Court."*

7. This Court in the case of *CANARA BANK GOLDEN JUBILEE STAFF WELFARE FUND vs. DEPUTY COMMISSIONER OF INCOME TAX* reported in [(2009) 308 ITR 202], while considering the general law relating to mutual concerns, has held at paras 13 and 14 as under:

> *"13. Under the general law relating to mutual concerns, the surplus accruing to a mutual concern cannot be regarded as income, profits or gains for the purpose of the Act (s.4), and where the contributors are to receive back a part of their own contributions, the complete identity between the contributors and recipients negatives the idea of any profit, for no man can make profit out of himself. Therefore, a mutual concern can carry on an activity with its members, though the surplus arising from such activity is not taxable income or profit. The principle of mutuality has also been accepted in the case of a voluntary organization, which receives contributions from its members.*
>
> *14. Thus, the crucial test of mutuality is that all the contributors to the common fund must be entitled to participate in the surplus and that all the participators in the surplus must be contributors to the common fund. In other words, there must be complete identity between the contributors and the participators. If this requirement is satisfied the particular form which the association takes is immaterial. Conversely, where there is no such identity between the class of contributors to the common fund and the class of participators in the surplus,*

the profits of the association would be assessable to tax."

8. The Tribunal in the case of *M/S. CENTURY CLUB IN ITA NO.205-207/BANG/2006, DATED 28.07.2006* has held that the provisions of Section 44AB of the Act had no application to the club and further held that even assuming the provisions were applicable, the appellant's bonafide belief that it did not required to get the accounts audited under section 44AB of the Act amounted to a reasonable cause for cancellation of penalty.

9. Indeed, these judgments referred to above, supports the contention of the assessee that Section 44AB of the Act is not applicable to the facts of the present case.

10. However, without entering into the issue of applicability of Section 44AB of the Act, if we examine as to whether the assessee had the bonafide belief which constituted reasonable cause to absolve him from the levy of penalty, it is clear from Section 273(B) of the Act that no penalty shall be leviable to a person or on assessee for any failure referred to

under the provision of Section 271B of the Act, if, it is proved that there was reasonable cause for such failure.

11. At this juncture, it would be beneficial to extract para 19 of the judgment of this Court in the case of *ASSISTANT COMMISSIONER OF INCOME TAX AND ANOTHER VS DR K SATISH SHETTY [(2009) 310 ITR 0366],* which reads as under:

> *"19. The Tribunal has also placed reliance on yet another judgment of the Supreme Court Hindustan Steel Ltd. vs. State of Orissa(1972) 83 ITR 26 (SC), where it dealt with the provisions contained in the Orissa Sales-tax Act. While considering the general principles the apex Court has held that penalty can be levied on failure of the assessee to get itself registered as a dealer under the Sales-tax Act only when it is established that he had not acted bona fide, or acted deliberately in defiance of law or was guilty of conduct contumacious, or dishonest, or in conscious disregard of his obligations. If the assessee was under a bona fide belief that it was not a dealer, them levying of penalty could not be justified. In view of the foregoing discussions, it is clear to us that the asessee had acted in bona fide belief and had no dishonest intention in not obtaining audit report for all the three businesses carried on by him".*

12. It is also relevant to extract para 7 and 8 of the judgment of Gujarat High Court in the case of *INCOME TAX OFFICE VS SACHINAM TRUST [(2010) 320 ITR 0445]*:

> *"7. In the circumstances, without entering into the analysis of provisions of Section 44AB of the Act, for the purpose of determining whether in the case of money lender, turnover would constitute the basis for invoking the said provision or gross receipts would constitute the basis for applying the said provision, the appeal is decided on the ground as to whether the assessee had a bona fide belief which constituted reasonable cause in the facts and circumstances of the case. Under the provisions of Section 273B of the Act, legislature has provided that notwithstanding anything contained in the provisions of Section 271B of the Act, no penalty shall be imposable on a person or an assessee for any failure referred to in the said provisions if it is proved that there was reasonable cause for the said failure.*
>
> *8. Therefore, without entering into the larger issue as to whether there was, or was not, any failure, it is apparent that the assessee can be said to have been prevented by reasonable cause on the basis of a legal opinion published, which was produced before the first appellate authority. In fact, on a reading of provisions of Section 44AB of the Act, it is a moot question as to which of the three phrases can be said to be applicable in a given case, and the same would depend on facts of each case and no straight jacket*

formula can be evolved in this context. Accordingly, the assessee was entitled to contend that when the terms turnover and gross receipts are separated by the use of word or, the assessee would be entitled to bonafidely believe that gross receipts would constitute the basis for ascertaining the limit of Rs.40 lakhs so as to attract Section 44AB of the Act."

13. The explanation of bonafide belief offered by the appellant would constitute a reasonable cause to absolve the appellant from the imposition of penalty under Section 271(B) if, examined in the light of the judgments of ***Sathish Shetty*** [supra] and ***Sachinam Trust*** [supra], coupled with understanding of the issue relating to Section 44AB of the Act. in the light of the judgment of the Apex Court in ***Young men's Association*** case [supra] vis-a-vis Section 2(13) read with Section 44AB of the Act, it could be safely held that the assessee had acted under a bonafide belief and there was reasonable cause in not obtaining audit report.

14. Thus, it is clear that the assessee was under the bonafide belief that the provisions of Section 44AB of the Act were not applicable to a Club, while supplying beverages, liquor

etc., to its members as it was not engaged in any business, but only a mutuality. The authorities and the Tribunal failed to appreciate the vital aspect of the explanation offered by the appellant in a right perspective and as such, in our considered opinion, the order passed by the Tribunal confirming the order of penalty is unsustainable.

15. For the foregoing reasons, we answer the substantial questions of law raised in these appeals in favour of the assessee and against the revenue. The impugned orders of the Tribunal and of lower authority imposing penalty are set aside.

Appeals are allowed accordingly.

Sd/-
JUDGE

Sd/-
JUDGE

*bgn/-