HVN 2008:BHC-OS:5163-DB

IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO. 121 OF 2005

The Commissioner of Income Tax -16
Mumbai. ... Appellant

Versus

M/s. Willingdon Sports Club,
Clark Road, Mahalaxmi,
Mumbai 400 034. ... Respondent

Mr. P.S. Sahadevan for the Appellant.

Mr.K.B. Bhujale for Respondent.

**CORAM: F.I. REBELLO &**
**R.S. MOHITE, JJ.**
**DATED: MARCH 18, 2008**

ORAL JUDGMENT (Per F.I. Rebello,J.):

. Revenue has preferred this appeal on the following substantial questions of law:

"(a) Whether on the facts and in the circumstances of the case and in law the Hon'ble Tribunal was right in holding that the entrance fees received by the Assessee is capital receipt not chargeable to tax as the principle of mutuality applies?

(b) Whether commuted value of subscription for the life members has to be taxed or treated as capital receipts in the light of the decision of the Hon'ble Bombay High Court in CIT Vs. WIAA Club reported in 136 ITR 569?

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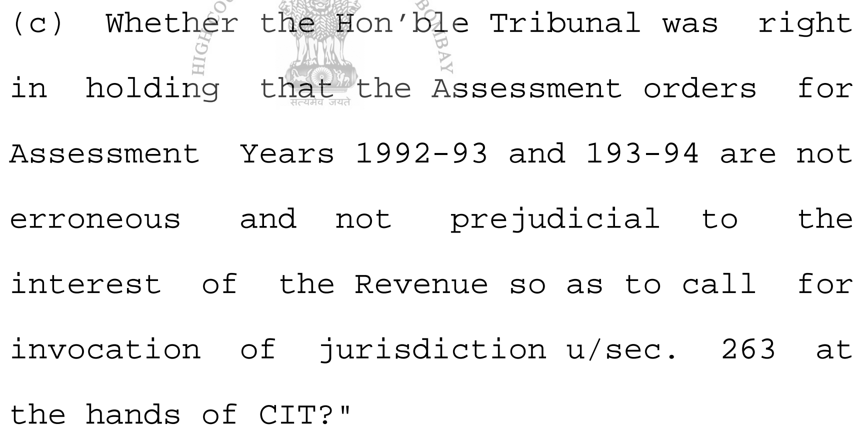
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(c) Whether the Hon'ble Tribunal was right in holding that the Assessment orders for Assessment Years 1992-93 and 193-94 are not erroneous and not prejudicial to the interest of the Revenue so as to call for invocation of jurisdiction u/sec. 263 at the hands of CIT?"

. A few facts may be set out :

. The relevant assessment year is 1992-1993. The respondent is governed by its rules and bye laws. Its members are described as Gymkhana Member, Corporate member, short term member all of whom are entitled to the advantages or privileges or membership of the club except that of being present or of voting at the General Meetings of the club or of serving on the General Committee and of proposing or seconding candidates for elections as members of the club. Apart from these members, there are life/founder/ordinary/super number members . The Assessing Officer pursuant to the return filed by the Assessee, assessed the total income at Rs.15,75,900/-.

2. In an appeal preferred by the Assessee, the Commissioner (Appeals) noting the two distinct kind of members, held that the first category of members who were not allowed to vote during the general body meeting were also not eligible to participate or share in the surplus of the club on its winding up and relying on the judgment of this court in CIT Vs.

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WIAA Club Ltd. Mumbai, 136 ITR 159 held that entrance fees and commutation of fees both has to be taken as revenue receipt dismissed the appeals. In regard to income from house property held the principle of mutality will not apply and that annual letting value would be taxable.as such the principle of mutuality does not apply and the surplus is subject to income tax. The matter was referred to the A.O. for fresh asesssment de novo.

3. The Assessee aggrieved by the order of 27.03.1997 of the Commissioner (Appeals) filed an appeal before the I.T.A.T. I.T.A.T. by its order dated 24.6.2004 partly allowed the appeal filed by the Assesseee. In so far as income from house property, I.T.A.T. relied on the judgment of the Supreme Court in Chelmsford Club Vs. C.I.T. (2000) 243 ITR 89 holding that the annual letting value of the club was not assessable to income tax under the head "income from house property". The tribunal in its order recorded a finding of fact that as per the objective of the club, it was not formed for the purpose of earning profit or for the purposes of earning profit or for the purposes of trading with the members and making a profit. In the matter of entrance fees and commutation fees the learned tribunal held that the entrance fees received by the Assesses is capital receipt not chargeable to tax in view of the decision in the case of CIT Vs. WIAA Club Ltd. 136 ITR 569 which has been followed by this court in CIT Vs. Diners Business Services Pvt. Ltd. (2003) 263 ITR 139. The appeal preferred by

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the Assessee was therefore, allowed and hence, the question is framed.

4. It is in this background that we shall have to answer the questions of law as set out in questions (a) and (b). The principle question to be answered is whether on the facts, the principle of mutuality applies and considering the judgment of this court in WIAA Club (Supra) whether the commuted value of subscription for life members has to be taxed or treated as capital receipt. In so far as issue of house property is concerned, the Revenue has not raised any question of law. The Learned tribunal basically relied on various judgments. There is however, a specific finding that the principle of mutuality applies and the entrance fees received by the Assessee is capital receipt not chargeable to tax. The principle of mutuality has been accepted in our jurisprudence. The principle can be summed up from Halsbury's Laws of England, Fourth edition, Reissue Volume 23:

> "Where a number of persons combine together and contribute to a common fund for the financing of some venture or object and will in this respect have no dealings or relations with any outside body, then any surplus returned to those persons cannot be regarded in any sense as profit. There must be complete identity between the contributors and the participators. If these requirements are fulfilled, it is

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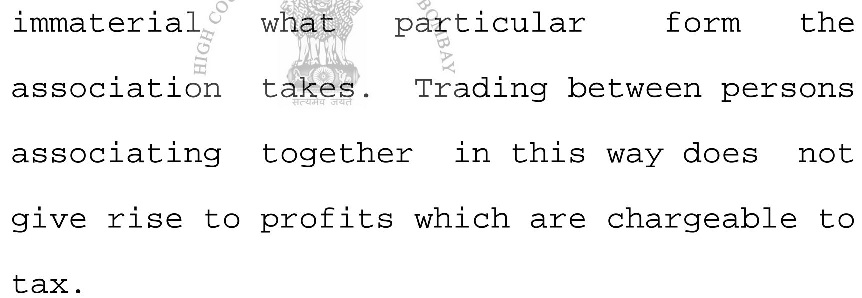

> immaterial what particular form the association takes. Trading between persons associating together in this way does not give rise to profits which are chargeable to tax.
>
> . Where the trade or activity is mutual, the fact that, as regards certain activities, certain members only of the association take advantage of the facilities which it offers does not affect the mutuality of the enterprise.
>
> . Member's clubs are an example of a mutual undertaking; but, where a club extends facilities to non-members, to that extent the element of mutuality is wanting....."

. The principle of mutuality, when the receipt by the club are exempt from taxation, based on a clause of mutality has been succinctly stated by the Judicial Committee of the Privy Council in Fletcher Vs. Income Tax Commissioner (1971)3 ALL ER 1985 at Page 1189 reads thus :

> "... is the activity, on the one hand, a trade, or an adventure in the nature of trade, producing a profit, or is it, on the other, a mutual arrangement which, at most, gives rise to a surplus?"

5. A similar issue came up for consideration before

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the Supreme Court in Commissioner of Income Tax Vs. Bankipur Club Vol.226 ITR 97. The issue referred by the High Court therein was whether the profits arising from sales made to regular members of the club are entitled to exemption on the doctrine of mutuality. There also there were various kinds of members like permanent, temporary as also Honorary members. The temporary and Honorary members enjoyed all the privileges of the club subject to such restrictions and regulations as being prescribed by the rules and bylaws of the club. They had however, no right to vote at the meeting or bring any guest. Another appeal was in respect of Ranchi Club where the issue was whether the income derived by the assessee club from house property let to its members and their guests is not chargeable to tax. The High Court therein had held that income derived by it from its members or their guests and sale of liquor to its members and guests was not taxable. There were several other appeals also. The main issue canvassed by the Revenue before the Supreme Court was as under :

> "Whether the assessee-mutual clubs, were entitled to exemption for the receipts or surplus arising from the sales of drinks, refreshments. etc. or amounts received by way of rent for letting out the buildings or amounts received by way of admission fees, periodical subscriptions and receipts of similar nature from its members?"

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. The appellate tribunal as also the High Court had recorded a finding that these amounts received by way of admission fees, periodical subscriptions etc. from the members of the clubs were only towards the charges for the privileges, conveniences and amenities provided to the members, which they were entitled to as per the rules and regulations of the respective clubs. It was further recorded that the facilities were offered only as a matter of convenience for the use of the members and their friends, if any, availing of the facilities occasionally. The services offered were not done with any profit motive and were not tainted with commerciality. In view of these findings the court held that the activity of the clubs cannot be considered to be trading activity and the surplus/excess of receipts over the expenditure as a result of mutual agreement cannot be said to be "income" for the purpose of the Act. The Supreme Court thereafter relying on various English decisions held as under :

> "We understand these decisions to lay down the broad proposition - that, if the object of the assessee-company claiming to be a "mutual concern" or "club" is to carry on a particular business and money is realised both from the members and from non-members, for the same consideration by giving the same or similar facilities to all alike in respect of the one and the same business carried on by it, the dealings as a whole

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disclose the same profit-earning motive and are alike tainted with commerciality. In other words, the activity carried on by the assessee, in such cases, claiming to be a "mutual concern" or "members club" is a trade or an adventure in the nature of trade and transactions entered into with the members or non members alike is a trade/business/transaction and the resultant surplus is certainly profit income liable to tax..."

. The court went on to observe that :

""at what point, does the relationship of mutuality end and that of trading begin" is a difficult and vexed question."

. The court then proceeded to hold :

"Whether or not the persons dealing with each other, are a "mutual club" or carrying on a trading activity or an adventure in the nature of trade", is largely a question of fact."

. It is thus discernible that in those cases where the facilities extended by the clubs to their members are as a part of usual privileges, advantages and conveniences attached to the members of the club, said activity can not be said to be trading activity. On the other hand, if the

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activities has disclosed profit earning motive and are tainted with commerciality, then it ceases to be mutuality and the very claim that the assessee is mutual concern of the members club wold be of no consequences.

. Once a finding is recorded that there is no commerciality and what is being offered are usual privileges, advantages and conveniences that would attract he principle of mutality. Such a finding and consequent applicability of the principle can not be interfered with unless Revenue from the record points out that the findings are totally perverse. In the instant case, as we have noted earlier, the Revenue has not disputed that fact. What is only disputed is whether the entrance fees received by the assessee is capital receipt and the commuted value of subscription for life members has to be taxed or treated as capital receipt.

6. The Revenue it appears have based their submission on the judgment of this court in Commissioner Vs. W.I.A.A. Club Limited, 136 ITR 569. The Membership of the club consisted of ordinary members and life members. The ordinary members were paying entrance fees and annual subscription. The Life members were paying larger entrance fees without any liability to pay annual subscription. The club was extending similar facilities both to ordinary and life members. The issue of mutuality was neither argued nor raised or was in issue before the learned Bench of this Court.

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It is on the facts there and without considering the principle of mutuality that the learned Bench proceeded to hold that the amount paid by the members had two elements in it. The part of the amount paid as entrance fees which were paid to the club with a view to acquiring the right to avail of the services and facilities extended by the club. The other part was a consolidated commuted payment in lieu of annual subscription. The court held that that part of the entrance fees which was a compounded payment for annual subscription would be income and the balance would be a capital receipt. In our opinion, considering the judgment of the Supreme Court in Bankipur (supra) an the issue of mutuality which has been raised in the present appeal, the judgment in W.I.A.A. Club (supra) is clearly distinguishable. Even otherwise, in our opinion, it is doubtful whether it would be correct law considering the judgement in Bankipur (supra).

. In Chelmsford Club Vs. Commissioner of Income Tax, Vol. 243 I.T.R. 89, the Supreme court observed that what is taxed is "income, profits or gains" earned or "arising", "accruing" to a "person". Where a number of persons come together and contribute to a common fund for the financing of some object and in this respect have no dealings or relations with any outside body, then any surplus returned to those persons can not be regarded in any sense as profit. There must be complete identity between the contributors and the participators. If these requirements are fulfilled, it is immaterial

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what particular form the association takes. Trading between persons associating together in this way does not give rise to profits which are chargeable to tax. The law recognises the principle of mutuality excluding the levy of income tax from the income of such business to which the above principle is applicable. In that case the assessee was registered as company under the Companies Act. It was however, contended that the business was governed by the principles of mutuality and therefore, income, if any earned is outside the scope of the Income Tax Act. This argument was based on the principles that it is only income which comes within the definition of 2(24) of the Act that can be taxed and this definition generally excludes the income from business involving the doctrine of mutuality, except the business that is included specifically in sub clause (vii) of that section. The issue there was whether the income from property of the said assessee was exigible to income Tax. The court there on facts found that the doctrine of mutuality would apply and consequently that income from house property would not be exigible to tax.

7. From the principles which have been set out above and more so in the judgment in Bankipur (supra), even if there be temporary or Honorary members who are not entitled to vote, the assessee would not cease to be governed by the principles of mutuality. Once the assessee is governed by the principles of mutuality, its income earned would not be income which would be assessable to tax.

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8. For the aforesaid reasons, we are of the view that there is no infirmity in the judgment and consequently the questions as raised are devoid of merit and consequently appeal dismissed.

(R.S. MOHITE, J.)                (F.I.REBELLO, J.)

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