

**IN THE INCOME TAX APPELLATE TRIBUNAL :  
CUTTACK BENCH : CUTTACK**

**(Before Shri N.L. Dash, J.M. and Sri P.P. Rajesh, A.M.)  
I.T.A. No. 125(CTK) of 2000 : Assessment year : 1997-98**

Bhubaneswar Club Ltd. ... Appellant  
-vs-  
Asst. Commissioner of Income-tax,  
Respondent  
Circle-I(I), Bhubaneswar

AND

**I.T.A. No. 117 (CTK) of 2000 : Assessment year : 1997-98**

Asst. Commissioner of Income-Tax, ... Appellant  
Circle-I(I), Bhubaneswar  
-vs-  
Bhubaneswar Club Ltd. ...  
Respondent

Assessee by : Shri S. K. Dash  
Department by : Shri B. K. Mohanty

**O R D E R**

**Per Shri R.P. Rajesh, A. M.**

This cross appeals are filed by the revenue and the assessee against the order of the Ld. CIT(A), Bhubaneswar passed on 28.12.2001 in respect of the assessment years 1997-1998. These appeals are heard together and are being disposed of by a common order for the sake of convenience.

2. The grounds taken by the assessee in ITA No. 125/CTK/2000 are as under

1. That the order dated 28.12.2001 of the learned Commissioner of Income-tax (Appeals)-I, Bhubaneswar is unjustified, arbitrary, pre-judged, against the weight of evidence on record and bad in law.
2. That the rejection of the applicability of the Principles of mutuality as claimed by the appellant on arbitrary assumption of the learned Assessing Officer and confirmed by the Commissioner of Income-tax (Appeals)-I, Bhubaneswar is bad in law and not evidenced.

3. That the rejection of books of account under section 145 of the Income-tax Act, 1961 is bad in law and not evidenced.
4. That the rejection of the standard accounting procedure adopted by the club is bad in law and not evidenced.
5. That the Capital receipts of Entrance Fees from members amounting to Rs.12,20,000/- and a Capital receipt of Rs.3,00,000/- from ITC Ltd. was arbitrarily held to be revenue receipt by the learned Assessing Officer and the same was confirmed while adjudicating the appeal by the learned Commissioner of Income Tax (A) is bad in law and not evidenced.
6. That the addition of a sum of Rs.36,350/- on entertainment account by disallowing a loss arising on this account to a tune of Rs.5,41,338/- is bad in law and not evidenced.
7. That disallowance of establishment expenses to a tune of Rs.1,78,000/- from out of a total claim of Rs.17,85,203/- and disallowance of losses arising out of card room, billiards, tennis and other games to a tune of Rs.1.24,556/- on an arbitrary basis is bad in law and not evidenced.
8. That the view taken by the Id. CIT(A) on the procedure adopted by the appellant for induction of new members is bad in law and not evidenced.
9. That the appellant craves leave to add, to amend any of these grounds before or at the time of appeal.

3. Before coming to the specific issues raised in various grounds it is necessary to narrate the facts in brief leading to present appeal. The assessee is a company duly registered under section 25 of the Companies Act, the liability being limited by the guarantee of the Members with the main objective of providing various conveniences as is given in clubs for use of its member and its guests with the cardinal principle of mutuality. Although the club is incorporated as a company, it is an entity and instrumentality for convenience of the members. The return for assessment year 1997-98 was filed on 20.03.98 disclosing loss of Rs.92,830/-, the AO examined the books of account and it was found by the AO that all necessary books of accounts were not available for verification in respect of receipt and expenditure. Therefore, the AO came to the conclusion that it is difficult and impossible to verify the correctness of all the expenses debited under various heads like entertainment account, repairing and expenses, staff welfare and printing and postage. The AO noticed that there was disproportionate and unjustified expenditure which could not be substantiated by the assessee. He also found certain other deficiencies in the books of account maintained by the assessee. The AO also noticed that the assessee has received a lump sum amount of Rs.3,00,000/- from

ITC Ltd. which was considered by the AO as revenue receipt. It was argued by the assessee that whether the receipt is capital or revenue is immaterial since its purpose was to support the club activity which is enjoyed only by the club members. The Id. AO further examined the claim of mutuality and came to the conclusion that the assessee has not been able to discharge its onus of establishing that all the receipts have flown from its members and that the participators in the privileges / conveniences and the contributors are identical. The Id. AO was of the view that the facility of Bhubaneswar Club was not restricted to its members only but non-members and outsiders have access to its benefits, services and privileges. It was also noticed by the AO that the guest room facilities which are its substantial sources of earning, are available not only to the members and their guests but also to the members of affiliated clubs. Such affiliated clubs cannot be claimed as contributors to the common fund in the status of member. Therefore, it is evident that even the normal activities of the assessee include those which geared to the non-members. As such, the AO came to the conclusion that the concept of mutuality is not applicable to the assessee's functioning and it can be simply concluded that the entire fees received by it from its members were revenue receipts. Finally, the Id. AO concluded that

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“In view of the detailed discussion made in the body of the order, the inability of the assessee to discharge its onus establishing, conclusive that it is a mutual concern where mutuality is evident from the manner of maintenance of books of account & records and the other related and circumstantial evidences discussed, it is therefore, reasonable to conclude that the activities of Bhubaneswar Club Ltd. are not in the nature of mutual activities between a group of members who are identical as contributors and participators in privileges/benefits/surplus. Merely having the nomenclature of a “Club” is not enough to prove that it constitutes a mutual undertaking. The claim must be rigorously established from the books of account by assessee and the receipts must be clearly identifiable member-wise. In fact, the books of account of the club should have been maintained with greater transparency and detail from which it could be easily and conclusively ascertained that all the receipts have flown from the members alone. This has not been done and, therefore, the club has been handicapped in substantiating its own claim of mutuality. If its claim of mutuality is accepted then any commercial restaurant, hotel, bar or entertainment centre offering its facility to the public could, on similar evidences and books of account, claim mutuality and consequent exemption of its profits. The assessee has, in fact, wrongly classified the various receipts from its members on account of entrance fee, development fee, mutual benefit Fee and collection from sponsors as capital receipts when the same do not contain any characteristic of a capital receipt. They are intrinsically linked to the normal activities of the Club and constitute revenue receipts as discussed and, therefore, are being considered as such in the computation of income.”

4. With the above observation, the AO proceeded to compute the total income as under :-

A.	1.Profit from Bar	Rs.7,30,990/-
	2.Profit from Kitchen/Restaurant	Rs.4,35,313/-
	3.Profit from Entertainment a/c.	Rs.36,350/-
	4.Profit from Guest room a/c.	Rs.2,47,414/-
	5.Profit from Card room, billiards, tennis & other games a/c.	-----
	6.Other revenue receipts	Rs.14,23,028/-
		Rs.28,73,095/-
Less :	Establishment & other charges as discussed (17,85,203/-- 1,78,000/-	Rs.16,07,203/-
		Rs.12,65,892/-
Less :	Depreciation as claimed	Rs.4,78,186/-

	Rs.7,87,406/-
B. Receipts from ITC as per discussion	Rs.3,00,000/-
C i) Entrance fee as per discussion	Rs.12,20,000/-
ii) Development fee as per discussion	Rs.6,63,375/-
iii) Mutual benefit fund (net) as per discussion	Rs, 82,000/-
Total income :	Rs.30,52,781/-
Or say :	Rs.30,52,780/-

5. When the matter came up before the CIT(A), the Id. CIT(A) rejected the claim of the assessee that the club is an assessee of mutual concern and its income is exempt. He held that the Assessing Officer was justified in rejecting the books of account and resorting to the provision of sec. 145. He, however, allowed relief to the assessee by deleting certain additions, hence, aggrieved by the order, the revenue is also in appeal before us with the following grounds :-

**I.T.A. No. 117 (CTK) of 2000**

“On the facts and in the circumstances of the case, the Ld. C1T(A) is not justified in deleting the addition of Rs.6,63,375/- representing development fees and Rs.82,000/- representing mutual benefit fund, when he has already held that assessee failed to prove the existence of mutuality.”

6. We shall take up first assessee’s appeal :-

6.1 The Id. counsel appearing on behalf of the assessee reiterated the submissions made before the CIT(A) and assailed the order of CIT(A). He also supported the order of Id. CIT(A) in deleting the addition of Rs.6,63,375/- representing development fees and Rs.82,000/- representing mutual benefit fund. The Id. departmental representative supported the orders of authorities below. He has filed written submissions, the relevant portion of which are reproduced below:

“2. Claim of exemption on the doctrine of mutuality :  
Background information

Though the assessee Company has been filing returns of income since long, there has been no claim for any exemption on the principle of mutuality in any of the Returns of Income. As such the issue of application of the doctrine of mutuality has never arisen on the case of the assessee in the past. For the first time for the assessment year 1997-98 this issue arose in the course of the assessment proceedings, and for the first time for this assessment year the assessee claimed that its income would be exempt since it was involved in the activities of mutual trading. The accounts filed by the assessee along with return for the assessment year 1997-98 are similar to those that are filed by the other assesses carrying on business, and there is no trace in those accounts of any mutual trading activities. In other words, from the accounts and documents filed with the return, it is not at all ascertainable that it is a Members Club, and the income/surplus generated from its various activities is not chargeable to tax because there is no profit earned by it in the commercial sense.

The question of applicability of the doctrine of mutuality arose during the assessment year in question because the accounts of the assessee company were for the first time subjected to thorough scrutiny in the hands of the Department, and in the course of such examination and verification, several defects in the accounts were noticed. All these defects have been very clearly and categorically brought out and discussed by the Ld. Assessing Officer (A.O.) in the assessment order and by the Ld. CIT(A) in the Appellate Order. The serious defects thus noticed from the accounts gave rise to a possibility of determining a positive income and charging of the same to tax. It is pertinent to mention here that the assessee has disclosed a loss not only in the return for the assessment year 1997-98 but for all the preceding years right from the year of filing of return.

The A.O. completed the assessment on 29.03.2000 u/s. 143(3) of the Income Tax Act rejecting the assessee's claim that its income would be exempt on the principle of mutuality, and computing the total income at Rs.30,52,780/- disallowing certain expenses partly and treating certain incomes claimed as capital receipts as revenue receipts. On appeal, the Ld. CIT(A) while upholding the decision of the A.O. to deny the benefit of mutuality to the assessee has allowed its appeal partly granting a relief of Rs.7,45,375/- by his order in ITA No. 11/Co/2000 dated 28.12.2001.

The aforesaid order of the Id. CIT(A) is now under challenge before the Hon'ble ITAT by both the assessee and the Income Tax Department.

3. Law relating to Mutual Trading or Mutual Undertaking or Members Club: Principle of Mutuality:

There is no provisions in the I.T.Act exempting the incomes of a mutual undertaking or members club. The principle of mutuality is based on the extended commonsense understanding that nobody can earn a profit by trading with himself. The law relating to mutual trading or mutual undertaking has been discussed in detail in the landmark decision of the Hon'ble Supreme Court in the case of CIT vs. Bankipur Club Ltd., 226 ITR 97.

The law relating to the principle of mutuality as per the above decision of the Hon'ble Apex Court is as follows :

1. Where a number of persons combine together and contribute to a common fund for the financing or some venture or objects, 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. Trading between persons associating in this way does not give rise to profit chargeable to tax.
2. For the doctrine of mutuality to apply, it is essential that all the contributors to the common fund are entitled to participate in the surplus, and, that all the participators in the surplus are contributors and participators. This means identity as a class.
3. Members Club is an example of a mutual undertaking, but where a club extends facilities to non-members, to that extent the element of mutuality is wanting.
4. It is settled law that if the persons carrying on the trade do so in such a way that they and the customers are the same persons, no profits or gains are yielded by the trade for tax purposes, and therefore, no assessment in respect of the trade can be made.
5. A Member Club is assessable in respect of profits derived from affording its facilities to non-members.
6. The arrangement of relationship between the club and its members should be of a non-trading character.
7. 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 realized both from members and non-members for the same consideration by giving same or similar facilities to all alike in respect of the one and the

same business carried on by it, the dealing as a whole disclosed the same profit earning motive, and are alike tainted with commerciality. In such cases, the activity carried on by the assessee is a trade or an adventure in the nature of trade, and as such, the surplus is certainly profit liable to tax.

8. At what point of time, does the relationship of, mutuality end and that of trading begin is a difficult and vexed question. A host of factors have to be considered to arrive at a conclusion. 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.
4. Assessment proceedings and information available in the assessment records.

Return of Income for this assessment year 1997-98 disclosing a loss Rs.7,39,460/- was filed on 20.03.1998. It is evident from the assessment records that the assessment proceeding in this case were initiated by issue of notice u/s. 143(2) on 16.03.1999. Subsequently notices u/s. 143(2) were issued calling for specific information and books of account. Hearings before the A.O. took place on various dates over a period of 12 months and the Order Sheet notings in respect of such hearings, as are found in the assessment record, clearly show that adequate opportunities were provided to the assessee to prove the various claims it had made in the return of income and the accompanying accounts. The various books of account produced by the assessee in the course of such hearings were also thoroughly examined and verified by the AO. The detailed and elaborate notes in the Order Sheet notings signed by both the AO and the Ld. A.R. of the assessee, are quite revealing in so far as they contain vital facts with regard to AO's findings on examination of the accounts, and the assessee's failure to produce certain important details and information.

I) Certain significant findings recorded in the aforesaid Order Sheet Notings may be mentioned below :

Order sheet notings dated 22.02.2005 and 27.03.2000

1. The memo numbers mentioned in the Kitchen Daily Sales Register do not contain the name or membership number of the persons/members who have taken food in the restaurant. This is merely in the nature of KOT (Kitchen Order Ticket) wherein identity of the service recipients is not given. In respect of credit sales which are listed in the register it is not possible to correlate

the memo numbers with the outstanding entries. Collection made against credit sales on subsequent dates are not supported by money receipts. The members merely pay cash at the counter and collect the outstanding memos in their names.

2. The above procedure is also adopted in the Bar with the difference that no memos are issued and only the total of the BOT (Bar Order Token) are entered in the peg-wise stock account. The member's name and his membership number are not mentioned in the BOT.

3. The Bank vouchers and supporting primary evidences such as bills, etc. are not available for verification. No journal vouchers or journal registers have been maintained by the assessee.

II) Written submissions filed by the assessee in the course of hearings on 06.09.1999 & 15.02.2000

In the course of hearings on dates mentioned above, the assessee is found to have submitted two written submissions / explanations in respect of various queries raised by the A.O. Certain other documents are also found to have been filed before the A.O. in the course of the hearings.

(A) Written Submission dated 06.09.1999

At Para - 8 of this Written Submission the assessee stated as under:

“The details called for by your learned self in respect of break up of the amounts received from members towards head of subscription, Bar, Kitchen, Card room, Billiards, entertainment, Guest room, Tennis and other games is very voluminous as the number of members is more than 1000.

To understand the same please kindly note the accounting procedure adopted for all the receipts :

a. Subscription fees (includes Development fees which is treated as capital receipt) the same is collected on monthly basis for which monthly bills are raised.

b. Bar and Kitchen

The bills are raised immediately after use of the facility and mostly cash is collected. As such it would be stated that no records are maintained for individual members but for Credit Sales and these too are maintained till realization of dues only. Therefore it is not possible to furnish any details of members using such facilities.

c. Card Room, Billiards, Entertainment Tennis & other games

The procedure for realization of these heads from members is same as above and especially .in respect of Entertainment it is fully on cash basis as such no details are available for individual member.

d. The details of Souvenir Collection (earlier year collection) are for a sum of Rs.2,59,500/- and the same is from earlier year”.

(All the embhasis supplied)

Vital information that the above Written Submission contain:

From the above submission it is crystal clear that the assessee company does not maintain any records showing member-wise collections from Bar and Kitchen. Even for credit sales member wise details are kept only till the dues are realized. The details of members using such facilities are not maintained. The same procedure is followed in respect of collections from Card room. Billiards, Entertainment, Tennis and other games. Especially in respect of Entertainment all the collections are by way of cash and, therefore, there are no records to show the collections from individual members.

(B) Vital information contained in the Written Submission filed by the assessee in the codurse of hearings on 15.02.2000.

1. The assessee company had got substantial amount from the IMFA Trust for development of a Swimming Pool in the Club premises. It is not ascertainable whether the so-called IMFA Trust is a member of the Club.

2. The assessee company had also got substantial amounts of more than Rs.3,00,000/- from ITC Ltd., Visakhapatnam, a non-member.

3. The Guest Rooms are let out not only to the members and their guests, but also to non-members like members of affiliated clubs.

4. The assessee holds functions for entertainment of its members and their families on various occasions such as New Year's eve and Republic Day eve etc. which are some time sponsored by outsiders. These outsiders such as Bagpipers at times pay the amounts to the assessee and at some other times defray the expenses directly.

5. The assessee published a souvenir in the year 1991 for which advertisements were collected from outside parties and non-members, and the outstanding amounts receivable on this account were being collected also in the subsequent years as would be evident from the accounts.

(C) Letter of ITC Ltd., Visakhapatnam dated 18.03.2000 addressed to the AO

The above letter shows that ITC Ltd. contributed substantial amounts for three consecutive years as aq sponsor of various functions celebrated by the assessee company and that all these amounts were debited in the accounts of ITC Ltd. under the head sales promotion.

No accounts of utilization of such funds were ever submitted by the assessee company to ITC Ltd.

(D) Letter of NICCO UCO FINANCIAL SERVICE LTD. dated 15.07.1996 addressed to the assessee.

This letter shows that the assessee has advanced a loan of Rs.12,00,000/- to the above company and is getting substantial amount of interest from them. The interest so received cannot be said to be out of any mutual trading activity.

(E) Ledger extract in respect of Bank Interest

This reveals that the assessee had received interest from NICCO UCO FINANCIAL SERVICES LTD. and certain Banks to the tune of Rs.6,30,114/- on loans and deposits. Such receipt of interest is not on account of any mutual trading activity, and hence, is chargeable to tax.

5. Reasons for which the Assessing officer has rejected the assessee's claim for exemption on the principle of mutuality."

1. The assessee has categorically expressed its inability to establish that the receipts shown under the heads of various activities such as Entertainment, Kitchen, Bar, etc. have flown only from the members. It has failed to discharge its onus of establishing that all its receipts have flown only from its members and that the participators in the privileges/conveniences and the contributors are identical.

2. On examination of the books of account and the submissions made in the course of hearings, the irrefutable conclusion that emerges is that the assessee cannot, and has not been able, to prove that the receipts under the various heads of activities have flown only from the members and that they alone have enjoyed the facilities and privileges offered by the club.

3. The books or account indicate that the club is operating more as a commercial venture and the concept of mutuality, with its cardinal principle of identity between the contributors and the participators, is not evident. This taint of commerciality clear goes against the very principle of mutuality which is claimed by the assessee.

4. The facilities of Bhubaneswar Club are not restricted to its members alone and the non-members/outsideers also have access to its benefits, services and privileges. For example, the Guest Room facilities which is a substantial sources of earning for the assessee is available not only to the members and their guests, but also to the members of affiliated clubs who are stark outsiders.

5. It is evident that even the normal activities of the assessee include those which geared towards non-members It has also been noticed in later years that the assessee club has let out its open lawns in the name of members for holding large parties on the occasions of wedding, etc. The hundred of guests who partake the facilities of the club, including the food catered by the Club's kitchen cannot be treated as ordinary limited guest within the meaning of Club's bye-laws. These are a few instances to show that the club's activities having strong commercial overtones.

6. A very strong argument against the claim of mutuality put forth by the assessee club was available in recent times when a group called "Dreamers", who were non-members, organized a function in the club's premises in which hundreds of outsiders/non-members participated and enjoyed the facilities and privileges of the club. It is another matter that some law and order problem broke out in the course of the above function resulting in substantial loss to the properties of the club. Though this incident did not happen during the relevant previous year, it shows very clearly that the club's services, kitchen and bar facilities, lawns and grounds etc. are usually accessible to outsiders and non-members. Therefore, the taint of non-mutuality in the activities of the club cannot be denied.

7. In providing, facilities of restaurant, bar, guest rooms, games and other recreational services the club is merely performing specific services for its members and to that extent cannot claim any exemption of its income in view of the strict provisions of section 28(iii).

6. Disallowance of certain expenses and treatment of certain incomes as Revenue receipts in the assessment:

The Assessing Officer has rejected the book results disclosed as per accounts resorting to the provisions of section 145 of the I.T.Act for the following reasons:

1. The primary and proper evidence in support of the entries in the books of account have not been properly maintained and most of them were not even produced for verification. While payments have been made to various parties both through bank and in cash, the relevant details such as bank vouchers, bills in support of purchases, primary documents such as kitchen order token, money receipts etc. could not be produced in support of all entries in the books of account. Only some of the cash vouchers were produced in evidence of cash out-goings but these did not cover the entire period of transaction.

2. No journal vouchers or journal registers have been maintained by the assessee even though the ledger account descriptions under all the heads repeatedly refers to journalized transactions.

3. From an examination of the accounts, even though the same are shown as audited, it is difficult and impossible to ascertain the correctness of all the expenses debited under various heads, especially entertainment, house keeping expenses repair and maintenance, staff welfare, printing and postage, etc.

4. Comparison with the expenses claimed under various heads for the earlier years shows that under certain heads such as entertainment the assessee has claimed abnormality high expenses for the year under consideration.

5. The receipt from the members are also not verifiable member-wise with reference to money receipts etc. The money receipts are also found not to have been maintained regularly;

After rejecting the book results u/s. 145 of the I.T. Act the Assessing Officer has made the following additions in the assessment:

1. Estimated the profit on entertainment account at 10% of the receipts of Rs.3,63,489/-.
2. Disallowed 10% of the expenses claimed as established charges and overheads (Total claim was Rs.17,85,203/- ) which comes to Rs.1,78,000.-
3. Treated the receipts of Rs.3,00,000/- from ITC Ltd. claimed as capital receipt as revenue receipt.
4. Treated the entrance fees received from members totaling Rs.12,20,000/- as revenue receipt rejecting the claim of the assessee to treat the same as capital receipt.
5. Held that the club's income from interest not being from any mutual activity is exigible to tax, relying on the decision reported in 221 ITR 379 and 171 ITR 504.
6. Treated the receipts of Rs.6,63,375/- towards development fees and Rs.82,000/- towards the mutual benefit fund as revenue receipts rejecting the claim of the assessee to treat the same as capital receipts.

The Assessing Officer has, thus, computed the total income of the assessee company at Rs.30,52,780/- and raised the tax demand accordingly.

7. Appeal before Ld. CIT (Appeals):

In his elaborate and well reasoned order dated 28.12.2001, the Ld, CIT(A) has confirmed the action of the AO on the following points:

1. Rejection of the claim of exemption on the principle of mutuality.
2. Rejection of the book result u/s. 145 and estimation of profit and disallowance of expenses under certain heads.
3. Treatment of the receipts under the head entrance fees and from ITC Ltd. as revenue receipts.

The findings of the Ld. CIT(A) on assessee's claim of mutuality are there in para-4.2, page-4 of the Appellate Order. The reasons given by the Id. CIT(A) to confirm the decision of the AO on this point may be summed up below:

1. Assessment records of the appellant clearly indicate that neither during the year under consideration nor in the earlier previous years, the appellant claimed the benefit of exemption of income for

the purpose of taxation under the principle of mutuality. In the Income Tax Return Form there is a specific space (Part-V of return form) which an assessee claiming exemption of Income must fill up. In the tax returns filed by the appellant club right from the assessment year 1994-95 it has never claimed any part of its income as exemption through Part-V of the Return Form.

2. No record is maintained to ascertain the amount received from each member for various purposes. In respect of expenses also member-wise accounts including expenditure vouchers are not available with the appellant.

3. Major activities of the club are Bar and Kitchen. In respect of these activities no records are maintained for individual members. Member-wise break-ups for receipts from guest rooms and games are also not available. Sale memos arising out of sales from kitchen, restaurant and bar do not bear the name of the members of the club.

5. It is noticed that the club has hired out its open lawns etc. in the name of members for holding large parties on the occasion of weddings and other functions. Hundred of guests including non-members who partake the facilities of the club including food catered by the club kitchen cannot be considered as ordinary limited guests.

6. Since the appellant has claimed that its income is exempt under the principle of mutuality, the onus squarely lies on it to produce records and documents to prove that the activities of the club are limited to its members only. Without any appropriate records evidencing the facts of existence of mutuality, it cannot be held that the activities of the club are limited to the members.

7. The income earned by the appellant club is the result of specific services performed for its members and non-members alike by way of providing facilities of restaurant, bar, guest room, games and other recreational services, and as such the income earned is taxable u/s. 28.

8. The appellant has relied upon the decision of the Hon'ble Supreme Court in the case of Bankipur Club Ltd. vs. CIT reported in 227 ITR 97. In that case the club provided facilities to the members only and accordingly, it was decided that the surplus arising out of such facilities was exempt from taxation. In the case of the appellant there is utter failure to prove the existence of mutuality and it is noticed that they provided

facilities to outsiders/non-members. All the participators are not contributors in the case of the appellant and hence, the decision of the Supreme Court cited above does not help the appellant in any way.

8. Points in dispute in the appeal filed by the Department in ITA No. 1 17/CTK/2U02:

While confirming the action of the AO on all the major points, the Ld. CIT(A) has allowed relief to the assessee to the extent of Rs.7,45,375/-. In the assessment order the AO has treated the receipts by way of development fees and mutual benefits fund contributions of Rs.6,63,375/- and Rs.82,000/-respectively as revenue receipts on the ground that the receipts have not arisen from extinguishments of any capital right or transfer of any capital assets, and accordingly, added the same to the income estimated in assessment. The Id. CIT(A) has deleted the above additions for the following reasons given in para-6.4 page-6 of the Appellate Order.

1. Since the funds, whether under the head development fees or mutual benefit have come to the account books from the members by way of their contributions and are used not for the business of the club but for the development/construction of the club and benefit of the spouse of the members in case of member's death, such receipts cannot be regarded as revenue receipts.

2. The AO appearing before him on one of the dates of hearing i.e. 14.03.2001 did not object to these submissions.

9. Reasons why the decision of the CIT (A) deleting the additions is not justified.

1. It is now well settled that in order to decide whether or not a receipt is a revenue receipt, its true nature and substance must be looked into. The classification of the receipt in the form of accounts is not of any importance in considering whether the receipt is taxable as revenue receipt. [Hoshiarpur Electric Supply Co. vs. CIT (1961) 41 ITR 608(SC)]. It is the true nature and quality of the receipt, and not the head under which it is entered in the account books, which would prove decisive. If the receipt is a trading receipt, the fact that it is not so shown in the account books of the assessee would not prevent the Assessing Authority from treating it as a trading receipt or revenue receipt. [Chowringhee Sales Bureau Ltd. v. CIT (1973) 87 ITR 542(SC)]. While determining the nature of the receipt, it is totally irrelevant to consider whether such receipt was utilized for creation of capital assets or for running the day to day affairs of business. In the case

of the assessee, since the above receipts were not in the nature compensation received for immobilization, sterilization, destruction or loss, total or partial, of a capital asset, the same cannot be treated as capital receipt [CIT v. Bombay Burma Trading Corporation(1986) 161 1TR 38(SC)].

2. The Id. CIT(A) is not justified in treating the impugned receipts as capital receipts especially when he has upheld the decision of the AO to treat the entrance fees as revenue receipts rejecting the assessee's claim to treat the same as capital receipts.

3. Once the claim of mutuality is denied, the receipts from members for whatever purpose would partake the character of revenue receipts, and hence, would be liable to tax in assessment.

4. There is no evidence on record that the AO did not object to the decision of the Id. CIT(A) in this regard at the time of hearing of appeal on 14.03.2001. However, the alleged no-objection of the AO, notwithstanding, the Id. CIT(A) should have properly appreciated the facts and law governing the issue, and upheld the taxation of the impugned receipts as revenue receipts in assessment.

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### P R A Y E R

Keeping in view the submissions made as above, it is respectfully prayed that the Hon'ble ITAT would be pleased to dismiss the appeal filed by the assessee and allow the appeal filed by the Department, and oblige."

7. The written submissions by Id. departmental representative was supplied to the assessee and the assessee has filed its reply. The same is reproduced below :

1. That the submissions made by the Department are in response to the notes of submissions given by the appellant inter-alia on its claim of mutuality.

2. That in Para-2, it is stated that the appellant for the first time assessed to income-tax for the assessment year 1997-98 and the appellant also claimed for the first time its income to be exempted for mutuality. Since the club was incurring loss and the losses were being computed, the consideration of mutuality; does not arise. Otherwise also, if for any reason a mutuality is not claimed for one assessment year, it does not prevent or estop, the appellant for a subsequent

assessment year to claim it as the rule of res judicata do not apply. It is also not factually correct that the scrutiny assessment is for the first year. Such an assessment was done for the assessment year 1995-96 where the loss was accepted. This fact is capable to be tested from the records of the department (see also internal page-5 of Annexure-6 of the Parawise Comments submitted by the department where it says that assessment for 1995-96 was assessed u/s. 143(3) and accepted the loss. In this assessment year the entrance fee was treated as capital but not as revenue.

3. So far as the mutuality is concerned the appellant continue to maintain that it is a mutual concern and this fact can be verifiable from the books of accounts produced on which the learned Assessing Officer on 15.02.2000 says to quote "The books of account on various activities of the CLUB are examined. Case is discussed". Thereafter on 22.2.2000, 27.3.2000 and 28. 3. 2000, it is open for the Assessing Officer to specific re-examination and to find out non-mutuality than traveling elsewhere denying on by reference so some other untested facts in other years. None of these allegations were confronted and therefore they are untested materials not admissible for making assessment.
4. In Para-4 it reiterated that the assessing proceeding were continued for the period of 12 months and the order sheet notings in respect of such hearing as are found in assessment records. The copy enclosed as Annexure-3 clearly shows that adequate opportunities provided to the assessee to prove the various claims it had made in the return of income and the accompanying accounts.
5. The present submission by the department says that "They are quite revealing in-so-far as they contain vital facts with regard to AO's finding on examination of the accounts, and the assessee's failure to produce certain important details and information are not only vague but untrue.
6. It mentions the order-sheet notings dated 22.2.2005 and 27.3.2000. There is no order sheet on 22.2.2005. In the order sheet dated 27.3.2000 it says on a point of time when there was no direction to produce certain account despite the fact that all the accounts were produced on 15.2.2000. The allegation that part of the accounts were not produced cannot be true. The copies of which such wanting alleged documents have been filed.
7. In the written statement it was clearly explained about the subscription fees, Bar and Kitchen, Card Room, Billiards, Entertainment, Tennis & other games and the details of souvenir

collection. It is the deduction of the D.R. to say that from the above submission it is crystal clear that the assessee company does not maintain any records showing member-wise collections from Bar and Kitchen. This is not correct. Copies of the personal ledger A/cs. Submitted at Annexure-4 of the assessee's written submission.

8. It is not correct to say that IMFA TRUST is not a member of the CLUB. It is submitted this is not an issue in this appeal and factually IMFA TRUST is a member. These enquiries would have been made in the assessment stage not by doubt of D.R. it is again for the first time raised that ITC Limited is not a member-please see Para 11 at page-9 of the assessee's written submissions.
  9. Letting out to members and members of affiliated Clubs is also a claim of mutuality. Matters mentioned in B-4 were about advertisement in souvenir were collected from the members and no verification has been made earlier.
  10. The statements made in Paras-C.D. & E are materials now raised and they were also not factually correct. If the funds of the mutual organization is invested for earning interest its character is not altered to result into non-mutuality.
  11. An argument of no-mutuality is about Dreamers Festival. They do not relate to the year and in fact it was the CLUB'S programme where a group was invited to perform.
8. The Id. counsel has also filed his reply to various issues raised by the authorities below which is reproduced below:

“1. The claim of the assessee-appellant, a member's club, whose liability is limited by guarantee, incorporated under sec. 26 of the Indian Companies Act, 1882 and subject to sec. 27 of the said Act (presently correspond to sec. 25 and 26 respectively of the Companies Act, 1956) is that their surplus on the doctrine of mutuality is not income as defined under sec. 2(45) of the I.T.Act.

2. The Assessing Officer misunderstood this claim as a claim for exemption under sec. 10 and denied it for the reason that the assessee has not discharged its burden. The authorities below held that the claim cannot be allowed as (i) sec. 145 applies to its accounts are rejected, (ii) there are contributions by non-members to the common fund as well as participation by them for which there is no material. The CIT(A) granted some relief which is under challenge. Both appeals by the assessee and Revenue are heard together.

3. Under the Income Tax Act, the emphasis is on the income as defined under sec. 2(45) of the 1961 Act, and has three faces (i) it is charged under sec. 5; (ii) assessed under appropriate head and (iii) to be computed in the manner prescribed after making allowances and deductions provided under each head and by giving effect to the exemption from tax granted under the other provisions of the Act or otherwise treated as excluded. There are however statutory deviations, tax cannot be imposed by some implications or interpretations on untested materials made by the Assessing Officer. To illustrate a presumptive income without being really earned or disallowing expenses even if spent actually. The assessments are done qua, an assessee, who apart from being enumerated like an individual, HUF etc. are also the institution or organisations who exist by its incorporation and operate by their object clause to achieve their objects, they also undertake activities that appear akin to activities which are taxable under different heads of income. The conflict between the claim of the revenue to tax and the denial by them of those activities which are not a part of their object and something else has been determined by Courts on the test of 'main' and 'subsidiary' objects. Surplus arising or accruing to such institutions is not regarded as income of the concern please see Bar Council of Maharashtra and Surat Art Silk "when agrees to contribute" funds for a common purpose (such as payment of annuities or capital sums) to some or all of them, on the occurrence of events certain or uncertain, and stipulates that their contributions so far not required for that purpose shall be repaid to them", are not traders (could be house owners, money lenders as well) and contributions returned to them be regarded as profits (Please see Styles 2TC 460 at page-471 HL). It is the identity between the contributors and the recipients (even if not complete) negates the notion of income, on the doctrine that none can make a profit from himself. Whether a mutual concern may trade with its members or not is yet not settled (please see Municipal Mutual Insurance Ltd. - 16 TC 430, 442) but the surplus arising is not income to be taxable. This can be so only if the statute taxes it.
4. The return need not be in cash, but by kind (in reducing the next years premium (Styles 2TC 460, Jones 11 TC 814) or by diverting the surplus (Ecentric Club). The principle of mutuality is extended to different institutions, such as voluntary social organisation.
5. The assessee is a "member club", where a number of persons combine together and contribute to a common fund for the financing of some venture or object and in this respect have no dealings or relations with any outside body. As part of the usual privileges, advantages and conveniences attached to the membership of the club, it extends various facilities to its members by way of (i) sale of Food,

refreshments, beverages (ii) Letting out the guest rooms and lawns (iii) Games and sports like tennis, billiards, cards, swimming pool, etc. the amounts received by the assessee-club are by providing the above facilities, by way of entrance (admission) fees, periodical subscription from the members for various activities of the club. The facilities/services are offered by the assessee-club as a matter of convenience for the use of its members, their family members and invited guests, done with any profit motive nor tainted with commercially. There is complete identity between the contributors and the participators. The activities of the assessee-club do not constitute trading between persons associating together so as to give rise to surplus, which can be regarded as profit-income liable to tax. No portion of the income or property is to be paid or transferred directly or indirectly by way of dividend, bonus or otherwise by way of profit to persons who at any time were or have been members of the club or to any one or more of them or to any persons claiming through any one or more of them

6. For the financial year ended on 31.03.1997, relevant to the assessment year 1997-98, now under this appeal, the assessee-club filed the return of its income declaring a net assessable loss at Rs.92,830. No part of the income is assessable in the hands of the assessee-club applying the doctrine of mutuality. The assessee-club maintains regularly Journal, Cash Book, General Ledger, Personal Ledger of the members - separately for (a) monthly subscription and (b) bar & kitchen dues, Bar Sales Register and Kitchen Sales Register supported by Bill/Cash Memo, Journal Voucher, Cash Vouchers, Purchase Vouchers, Bar Order Tokens (BOT), Kitchen Order Token (KOT), Members Bill Register supported by the Bills issued to the members for the monthly dues payable by them, Guest Register, Guest Room Register. All the above books of account along with other relevant vouchers and documents were produced before the learned Assessing Officer to show that nothing is paid by non-members. In fact, on good faith, they were left with the learned Assessing Officer for about three months to facilitate examination of the transactions by the Income Tax Authorities. Photocopies of KOT, Bar Sales Register and Kitchen Sales Register, as a sample, were also submitted to the learned Assessing Officer. There is a distinction between 'income', 'exemption' and 'expenditure'. In CIT v. Cal. Hospital-57 ITR 313 (SC) when it was by specific enumeration u/s. 2(24)(vii) the transaction was taxable. Therefore, any transaction beyond mutuality is taxable. Trade or professional association may also be mutual concern.
7. The learned assessing officer attempted to make out a case on various grounds and dislodged the assessee-club's claim as a mutual-concern,

treating the receipts of Entrance Fees in the sum of Rs.12,20,000 ; Development fees in the sum of Rs.6,63,375 and Mutual Benefit fund in the sum of Rs.82,000 as income of the assessee-club. Further, the learned assessing officer treated the receipts of Rs.3,00,000 from ITC Ltd. as revenue receipt on an observation that rightfully the above receipt is not a receipt to construct a capital asset specifically but a receipt towards allowing ITC to use the club's prime display space for promotion of the ITC brand image". The learned assessing officer found fault with the assessee-club in maintaining the books of account and other related documents and accordingly rejected the assessee-club's books of account under sec.145 of the I.T.Act and estimated the income. Consequently she computed the assessee-club's total income at rs.30,52,781 as against the net loss of Rs.92,830 and brought the above income into the tax net.

8. In the assessee-club's appeal, the learned Commissioner (Appeals) mostly agreed with the findings of learned assessing officer on issues connected to the exclusion of the principles of mutuality, receipts from ITC Ltd. and the estimation of income, and consequently sustained the additions on those accounts. However, he deleted the additions of the receipts on account of Development Fund and Mutual Benefit Fund as an investment in mutual fund.

#### SUBMISSIONS-VIS-A-VIS-FINDINGS OF THE LOWER AUTHORITIES :

##### 9. RE: MUTUALITY

- a) It is submitted that the facilities offered by the Club are confined only to its members and their family members and guests .The guests are to be accompanied by a member or by an invitation from him and they do not have the privilege or independent entry. This is the practiced in the case of this club and nothing is found to say that some contributions are from non-members. No non-member is allowed to the facilities/services of the club unless introduced and accompanied by a member. Therefore, the question of receiving any amount from a non-member does not arise. The settled law about this receipt is non taxable when these persons form themselves into a company and arrange their affairs in such a way that the company makes profit for and on behalf of the members, it has got a distinct and separate personality from the members in the eye of law, but the members are using the company and the corporate personality for obtaining goods and services. The surplus that the company gets is held on behalf of the members and for future use of the members. The members may get it back either in the shape of reduction of price or extension of facilities that are to be provided to the members in future. The

important point is that the company is not acting as a business concern or a trading company on its own for the purpose of making gain. The company is being used by the members' for the purpose of obtaining goods and services as their agent. A company can make profit out of its members when members are treated as customers. Where, however, all that a company does is to collect money from a certain number of people and retain the surplus fund for the benefit of those people not as share holders of the company but as people who subscribed to it or plaid for it, then there is no profit. If the people were to do the thing for themselves, there would be no profit and the fact that they incorporate a legal entity to do it for them makes no difference. There is still no profit. This is not because the corporate entity of the company is to be disregarded, but because there is no accrual of profit, the money is simply collected from the members and held on their behalf, not in the character of shareholders but in the character of those who have paid for it. The excess that is realised from the members will be used for the benefit of the members in some form or other.

b) Claim in the form of Return.

The claim of mutuality is a factual claim keeping in view the principle that no person can trade with himself. There is no specific provision in the Income Tax Act for exempting the income of a mutual enterprise from the tax net. It is the judicial dictum which made the doctrine of mutuality operative on the mutual associations clubs. Therefore, the question of claiming the exemption of the assessee-club's income at Part V of the Form of Return does not arise. The learned assessing officer's observations recorded at Para-4 of page-4 of the assessment order that "in the returns filed by the assessee from Asst. Year 1994-95 onwards it has never claimed any part of its income as exempt in Part-V of the return form" is improper, unjustified and devoid of any merit. The assessee-club is entitled to claim any deduction/exemption in course of the proceedings for assessment or in appeal, and so it has rightly claimed for the application of the principles of mutuality at the assessment proceedings.

c) Bar and Kitchen Services

The BOT and KOT are made out by the waiter while taking orders for supply of beverages and food. The items and the quantities thereof are altered on many occasions. However, the bills are prepared for the actual items and their quantities supplied. It is a common knowledge that no person pays for an item or its quantity which is not served to him and the assessee-club is no exception to it. The bill raised evidences for the actual item and its quantity supplied which is also paid for. Commonly no where cash sales are backed by money receipt

nor do they contain the name of the purchaser. The assessee-club provide the facilities/privileges to its members and so it receives the money from the members only. It cannot receive any amount from a non-member even though such non-member is entertained as a guest of a member. Therefore, the question of receiving any amount from a non-member being a guest does not arise. All the cash sales at the bar and the restaurant are related to the assessee-club's member(s) only. Non-mentioning the name or the membership number of the member on the cash memo does not lead to infer that such sales were made to non-members. The sales registers, simultaneously contain a list of the members to whom credit sales are effected. At the end of each month separate bills are raised on the members to whom supplies are made on credit and the concerned members have also honoured the bills. The assessee-club maintains personal ledger account which inter-alia contain the date, the money receipt numbers and the amount received from the member. Therefore, the observations of the learned assessing officer at para 1 and 2 at page 5, of the assessment order as reproduced hereunder are improper and unjustified.

“In fact from the primary registers maintained in respect of the kitchen/restaurant and the two bars, it is impossible to arrive at a definite conclusion that the benefits have been enjoyed only by the members. The memos/bills and the kitchen order token (KOT) which are the primary documents in support of each transaction of sale in the restaurant do not mention the name of the membership no. of the members who have availed the facilities/privileges against their fees. The cash collections made towards the daily sales in the restaurant are not evidenced by money receipts. The credit sales/outstanding amounts listed daily in the kitchen sale register cannot be co-related with any particular memo/KOT so that it is not possible to verify which member availed the facilities for what amount, how much was received from him and/or outstanding in his name and the date on which the same was cleared up. In respect of the credit sales, the collections ostensibly made on a later date are not evidenced by money receipts or any other evidence indicating the identity of the payer.

Similar procedure, as in case of the kitchen sales, is adopted in the two bars also where the primary evidence of each transaction i.e. the bar order token (BOT) does not contain details or identity of the person who has utilized the privileges or partaken of the facilities offered by the club. In fact, in the bar section even memos are not raised and the entire transactions are accounted for in an ad-hoc manner by entering the total consumption quantity as per the BOT at the end of the day in the stock a/c. Likewise in the entertainment activities also the receipts are fully on cash basis and no details are available for individual members”.

Consequently the learned assessing officer's conclusion at Para-3 of Page-5 continued at Page-6 of the assessment order that the books of account indicate that the club is operating more as a commercial venture and the concept of mutuality, with its cardinal principle between the principle of identity between the contributor's and participators, is not evidenced and is not correct.

d) Guest Room Facility

The assessee-club has a set of rooms fully furnished and it provides accommodation to members, their families, the guests of the members and members of the affiliated clubs where reciprocity is there in those clubs. It also provides food & refreshments to them. The assessee-club charges rent for the room and also for the other facilities. The facilities including accommodation are provided by the assessee-club on behalf of the members and not as owner of the house property. The members had/have provided for themselves these facilities through the instrumentality or agency of the club. The assessee-club is not the landlord and the members, during their stay, are not the tenants of the club.

e) Hiring of Lawns, etc.

To dislodge the claim for the application of the principle of mutuality the learned assessing /officer has taken the cue from the events which occurred at the assessee-club premises in the years subsequent to the years which cannot be applied to the year under this appeal.

The assessee-club, in the later years, has let out its lawns to the members on the occasions of any celebration connected to them on their family members only. The assessee-club only caters food/refreshment to the members' invitees-outside caterers are not allowed into the club premises. For this purpose the concerned members-requisitionist is required to specify the nature of the function in his application for permitting him to use the club premises. The "Dreamfest", which has formed part of the orders of the lower authorities to destroy the principles of mutuality, was organised by the assessee-club for the entertainment of its members, in which a cultural organisation named "Dreamers" organised music and dance by the students of various Universities in the State of Orissa. Therefore it is submitted that the assessee-club has not allowed any non-member to use its premises at any time.

f) Performing Specific Services

Providing facilities of restaurant, bar, guest rooms, games and other recreation services by the assessee-club to its members does not constitute the performance of specific services by the assessee-club for its members as categorised by the learned assessing officer at the continuing Para 3 of Page 6 continued as Page-7. The Apex Court in the case of Bankipore Club Ltd. and many other Hon'ble High Courts have not held that providing the above facilities by a members' - club would constitute the performance of specific service.

The words 'performing specific services' means, 'conferring particular and tangible benefits' on the members which otherwise would not be available to them as such except for payment received by the association in respect of those services - CIT v. Calcutta Stock Exchange Association Ltd. (1959) 36 ITR 222 (SC). Specific services are performed by trade, professional or similar association but not by members' club.

- g) On the facts and in the circumstances stated here in above, the assessee-club humbly submits that there can be no argument that a club which is incorporated as a company has a personality separate and distinct from the members and, therefore, sales of goods and services to the members will amount to business activity of the company with another person and, in the eyes of law, it is earning profit just as an ordinary tradesman by selling goods to his customers makes profits and thus it has wholly discharged its onus of proving its claim of mutuality.

10. Re: ENTRANCE FEE

The normal accounting system is that the entrance (admission) fees received in large sums are treated as Capital receipts. The assessee-club receives the entrance fees from its members in large amounts and so it has not committed any error in treating them as capital receipt.

11. RE : RECEIPT OF Rs.3,00,000 FROM ITC LTD.

The ITC Ltd. is a corporate member of the assessee-club bearing No.C0011/01{"01" indicates one nominee). Therefore, the above receipt is from a member of the assessee-club. The assessee-club utilising the above amount constructed a permanent cabin with an open verandh to serve the purpose of a kitchen and open bar which is a capital asset. The advantage derived by the ITC by providing the above amount does not change the character of the receipt in the hands of the assessee-club.

## 12. RE: ESTIMATION OF INCOME

a) All the documents described at para-A.2 were produced before the learned Assessing Officer. It is for the learned Assessing Officer to check the books of A/C and other documents. The difficulty and/or impossibility to verify the accounts is not a ground to disbelieve the correctness of the accounts.

Para -1 of Page -5 of the Assessment order states that the Kitchen Order Token (KOT) does not bear name or membership number of the member. That means the learned Assessing Officer has verified the KOT & hence it is not justified to allege that they were not produced.

The increase or decrease in the expenses incurred as compared to the earlier year depended on the type and the volume of the activity carried on. During the year the assessee incurred expenses on holding musical and other programmes on 'housie'. Quiz and other competitions, April Fool Day, Holi, Judo Demonstration, Fashion Show, Independence Day, Diwali, New Year Day, etc. which are debited to 'Entertainment A/C'. The expenses so incurred are nor commensurate nor they are proportional to the collections from the members and/or sponsors.

The assessee-club has not collected any amount from its members on the above programmes, except in holding the New Year Eve for which a few members made specific contributions and the programme was enjoyed by many of the members. To facilitate the members and their guests to dine at the site of the entertainment, the assessee club issued separate coupons (termed in the accounts as Ticket sales) in place and instead of usual Cash Memo/Bill. The bifurcation of the receipts reflected in Entertainment A/c is given hereunder:-

<b><u>A) Sale of Food and Beverages</u></b>	<b><u>Rs.</u></b>	<b><u>Rs.</u></b>
20.07.1996	4,844	
30.08.1996	10,735	
31.01.1997	<u>35,560</u>	51,139

### **B) Sponsors**

Date	Name	Membership No.	
21.09.1996	Cadet		5,000
17.12.1996	SuperSalesCorporation		4,000
Sri V.K. Dhavan			
28.12.1996	Alpic Finance Ld.		10,000
30.12.1996	Aditya Steel	L0295	5,000

(Sri P.L.Kondo, Mg. Dir of

the company is a life Member)

30.12.1996	Sri R.S.Bhatia	L0260	3,000
01.01.1997	I'TC Ltd.	C0011/01	25,000
01.02.1997	East West Corporation		6,000
02.02.1997	Sri N.R.Patnaik	C0017/02	5,000
06.02.1997	Horberson Ld. (the	C0075	20,000

Company's distributions-

M/s.Utkal Distributions

are Corporate members)

12.02.1997	Spencer & Co.Their representative Sri P.K.	CP082	5,000
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Mohapatra was a member

12.02.1997	Nicco Uco F.S.L.	OP023	25,000
09.03.1997	Misc,-charges		3,000

1,16,000

C) Sale of Tickets to members for dinner, etc.  
on New Year Eve/Disco

24.12.96	4,450
25.12.96	2,550
26.12.1996	3,900
27.12.1996	2,800
27.12.1996	9,525
28.12.1996	17,450
28.12.1996	12,400
29.12.1996	11,850
29.12.1996	23,600
29.12.1996	500
30.12.1996	16,425
30.12.1996	26,700
31.12.1996	16,300
31.12.1996	34,700
04.01.1997	300
	270

1, 83,720

D) Collections on Housie on 8.2.1997 130

E) Refund of Stage charges - 22.1.1997 10,000

Picnic Expenses - 8.2.1997 2,500

Total: 3, 63,489

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All the sponsorers are members of the assessee-club either directly or through their proprietor, partner(s), director) s), agent or employee representative. The membership numbers of the members as readily identified, have been mentioned,

Therefore the Entertainment A/c cannot be subjected to estimation of profit.

A careful perusal of the 'Net Revenue Account' for the year would show that the expenditure on Electricity increased to Rs.3,54,281.30 as compared to Rs.1,78,088.80 in the financial year 1995-96. A comparison would further show that all other expenses are more or less equal to the preceding financial year 1995-96. Therefore the following findings of the learned Assessing Officer are improper and unjustified.

- (i) Primary and proper evidence in support of entries in the books of accounts have not been properly maintained
- (ii) Bank Vouchers, bills in support of purchases, primary documents such as Kitchen Order Tokens, Money Receipts etc. could not be produced in all the entries in the books of account.
- (iii) Only some of Cash Vouchers were produced in evidence of Cash outgoings but these did not cover the entire period of transaction.
- (iv) No journal voucher or journal registers have been maintained even though the ledger account descriptions under all the heads repeatedly refers to journalised transaction.
- (v) From an examination of accounts, even though the same are shown as audited, it is difficult and impossible to verify the correctness of all the expenses debited under various heads, especially substantial expenses under the head of entertainment account (Rs.9,04,827/-) house keeping expenses (Rs.1,092,266/- ), repairs & maintenance (Rs.3,44,052/-), staff welfare (Rs.57,516/- introduced for, the first time in the account) printing & postage (Rs.1,01,254/-), etc.
- (vi) The outgoings under a number of heads of expenditure are disproportionately higher in this year compared to the earlier years and the trend of receipts. In the entertainment account where a huge/loss of rs.5,41,338/- has been posted the

expenses are claimed at Rs.9, 04,827/-against receipts of Rs.3, 63,489/-. In the financial year 1995-96 the expenses were Rs.11,94,529/- against receipts of Rs.10,01,957/-. The disproportionate enhancement of expenses, given their unverifiable nature, could not be satisfactorily explained by the A.R. The receipts are also not verifiable member wise with reference to money receipts, etc. which have not been maintained regularly.

- b) The Tennis Account would show that (i.e) expenditure on staff salary has increased by about 50% whereas the collection from members has decreased by about 17.4% as compared to those in the financial year 1995-96. The Court and the equipments have to be maintained irrespective of the number of players.
- c) In Card Room there is little variation in the net loss.
- d) In 'Billiards' the collection from the members has substantially decreased in this year as compared to the preceding year and correspondingly the expenditure also decreased. The increase in the net loss attributes to the increase in the staff salary.
- e) The expenditure on 'Oiler Games' comprise of the expenditure on holding friendly cricket matches between the members of the assessee-club, for which it has not collect any separate subscription.
- f) The assessee-club consistently follows the mercantile method of accounting, which is not, disputed by the learned Assessing Officer. The accounts are also not defective as pointed out by the lower authorities. Therefore the application of section 145 doesn't arise.
- g) For the reasons set forth above, the rejection of the book results by the lower authorities is unjustified.

### 13. RE: MUTUAL BENEFIT FUND AND DEVELOPMENT FUND

The assessee-club collects subscriptions from its members towards Mutual Benefit Fund and Development Fund every month by raising a common Bill on each member. It maintains a separate personal Ledger Account of each category of the membership for the monthly dues/subscriptions receivable from individual member, Permanent Members, Corporate Members and Outstation Permanent Members.

At 8<sup>th</sup> line of the continuing paragraph of Page-5 of the assessment order it is clearly stated that "*it was verified that member-wise register has been*

*maintained for such receipts only.”* The CIT (A) has not committed any error in deleting the additions vide his order at para 6.4

14. RE: ELECTION TO MEMBERSHIP

It is for the assessee-club to decide its primacy and priority as regards the grant of membership and any deviation does not destroy the mutuality.

15. The following cases apply to the assessee.

- New York Life Insurance Co. vs. Styles (Surveyor of Taxes) - (1889) 2 TC 460 (HL)
- Jones vs. South West Lanchashira Coal Owners’ Association Ltd. - (1926-1927) 11 TC 814
- CIT v. Bar Council of Maharashtra - (1981) 130 ITR 28 (SC)
- CIT vs. Merchant Navy Club - (1974) 96 ITR 261 (AP)
- CIT v. Madras Race Club - (1976) 105 ITR 433 (Mad)
- Presidency Club Ltd. v. CIT- (1981) 127 ITR 264 (Mad)
- CIT v. West Godavari District Rice Millers Association - (1984) 150 ITR 394(AP)
- CIT v. Darjeeling Club Ltd. - (1985) 153 ITR 676(Cal).
- CIT v. Cochin Oil Merchants Association- (1987) 168 ITR 240 (Ker)
- CIT v. Bankipur Club Ltd. - (1997) 226 ITR 97 (SC)
- CIT v. Cement allocation Co-ordinating Organisation - (1999) 236 ITR 553 (Bom)
- Chelmsford Club v. CIT - (2002) 159 CTR (sc) 235”

9. Various findings recorded by the Ld. CIT (A) have been replied by the assessee which are as under:-

<b>Findings of CIT (A)</b>	<b>Assessee's comments</b>
1. The appellant did not claim the benefit of exemption of income for the purpose of taxation under the principle of mutuality, neither during the year under consideration nor in the earlier previous years. In the IT return form there is a specific space (Part V of the return form), which an assessee claiming exemption of income must fill up. The assessee has never claimed any part of its income as exempt through Part V of the return form.	The question of claiming the benefit of exemption from Income Tax did not arise as there was no “income” of the Club filed in the return and in fact the Club sustained loss as in the past.
2. No record is maintained to ascertain the amount received from each member for various purposes. In respect of expenses tool, member-wise accounts including the	It is totally incorrect statement. It is figment of imagination of the Revenue that without maintenance of member-wise accounts and relative accounts, and

<p>expenditure vouchers are not available with the appellant. No records are maintained for individual members for major activities of the club, i.e., bar and kitchen. Member-wise break up for receipt from guest room and games are not available. Sale memos arising out of sales from kitchen, restaurant and bar do not bear the names of the members of the club.</p>	<p>member-wise break up of account under Bar and Kitchen as well as others, accounts cannot be complete. All primary accounts details were produced and they were kept for long periods with the revenue and without giving opportunity to clarify any doubts arising out of the same, the Revenue chose to make above sweeping / arbitrary statement.</p>
<p>3. The club has hired out its open lawn, etc. in the names of members for holding large parties on the occasion of weddings, other functions, etc. Hundreds of uses including non-members who partake the club including food catered by the club kitchen cannot be considered as ordinary limited guests. It is the responsibility of the appellant alone to produce those records and documents to prove that the activity of the club is limited to the members only. Without any appropriate records evidencing the fact of existence of mutuality, it cannot be held that the activity of the club is limited to the members.</p>	<p>The Club vests certain inherent rights and privileges to its Members they have legitimate right to hire out Club lawns for holding parties or even large parties on occasions as appropriate to the requirements and hiring out of lawns by the Club for such requirements of its Members is not a violation of the principle of mutuality on the plea that the host members entertain their authorised guests. So long as the host member responsibility of the makes the payment for such hiring out lawns where his guests were also entertained, the violation of the mutuality principle does not arise. It is a settled law that “merely because the Club even if entered into transactions with non-members and earned profits out of such transactions, the Club’s right to claim exemption on the principle of mutuality in respect of such transactions held by it with its members is not lost and such income is not taxable”. The concept of “ordinary limited guests” as conjured and advanced by the revenue is not a workable or feasible proposition in a social club having membership of more than 1000 members and that cheap and economic food/beverage facilities are made available to members and their guests. The Supreme Court of India lie Id in the case of Bankipur Club Ltd., that where the “trade or activity is mutual, the fact that some members take advantage of the facilities which it (club) offers does not affect the mutuality of the enterprise”. This has been cited by the same Supreme Court of India in the case of</p>

	Chelmsford Club vs. CIT and the said Court endorsed the same in favour of the Club.
4. AO cited that a function out on 4.3.2000 (which is not within assessment year under appeal) under the aegis of “dreamers” and that neither the participants of the function nor most of the organisers were members of the club. The club has let out its lawns and club services to non-members and as such AO and CIT(A) opined that the principle of mutuality is not applicable and the income any income of the club is not free from taxation. Such income earned is taxable u/s. 28.	The revenue’s arbitrary depiction of the “Dreamfest” Cultural Function of the “Dreamers” (a Cultural Organisation) held in the Club for the benefit of the club Members, free of charge, to prove the point against the Club’s mutuality principle is totally irrelevant to the contentious issue for twin reasons that the event was held after the year under assessment and that the Club has the inherent right to hold cultural functions for the benefit of its members. Since the Club did not earn any income for holding the dreamfest cultural event, the taxability u/s. 28 does not arise.
5. In the instant case, the appellant failed to prove the existence of mutuality on the ground that the club provided facilities / services to outsiders / non-members. All the participators are not contributors and hence the club’s reliance upon the Hon'ble Supreme court’s decision in the case of Bankipur Club Ltd. (226 ITR 97) does not help the appellant.	<p>The Revenue’s contention that the Hon’ble Supreme Court’s decision in the case of Bankipur Club Ltd. (226 ITR 97) does not help the appellant is totally fallacious and oblivious of the legal realities. The Club conforms to all the requirements adjudicated in the case. In fact the Club’s claim for mutuality principle all the found further support in same Apex court’s decision in the case of Chelmsford Club Ltd., wherein the Apex Court clarified that there is clear identity between the contributors and the participators to the fund and the recipients thereof respectively based on when the question of the principle of mutuality could be tested with the following three conditions :</p> <p>i) The identity of the contributors to the fund and the recipients from the fund;</p> <p>ii) The treatment of the Company, though incorporated as a Club as a mere entity for the convenience of the members and their guests, in other words, as an instrument obedient to their mandate; and</p> <p>iii) The impossibility that contributors should derive profits from contributions</p>

made by themselves to a fund which could only be expended or returned to themselves.

Hence the Club's facilities are also open to guests of members and those guests cannot be treated as outsiders for the purpose of applicability of mutuality principle of the club. So long as the Club's services provided to the Members and their guests are paid by the host members, the question of violation of the principle of mutuality does not arise, besides the fact that Club does not transact any activity with any of the Members' guests without the host member of the club and as such taint of non-mutuality of the Club does not arise.

It has been clearly stated that the assessee company (club) is formed with the main object of providing various conveniences / privileges for use of its Members and their friends. The High court, Patna summarised in the head-note [(1992) 196 ITR 137 (Pat):38R.576 at page 139]

“... that merely because the assessee-company had entered into transactions with non-members and earned profits out of transactions held with them, its right to claim exemption on the principle of mutuality in respect of transactions held by it with its members was not lost. The assessee was a mutual concern. The income derived by it from its house property let to its members and their guests and from the sale of liquor, etc., to its members and their guests was not taxable in its hands.”

If we apply the above criteria to the facts of the case in hand then we find that the Club's business is governed by the doctrine of mutuality. It was stated in the case of the CIT vs. The Bankipur Club Ltd., the Supreme Court of India recognised the following excerpt from its judgment

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	<p>“Where the trade or activity is mutual, the fact that, as regards certain activities, certain members of the Club only take advantage of its facilities which it offers does not affect the mutuality of the enterprise”. The revenue failed to take cognisance of the Apex Court’s views and accept the claim of the Club for Mutuality Principle.</p>
<p>6. While computing the total revenue income and expenditure of the assessee, the A.O. did not accept the net loss arrived at by the club’s statutory auditors; instead Id. A.O. estimated the net profit by reducing the expenditure to camouflage expenditure at 10% of the gross receipts under the head of account i.e. entertainment and certain others. The Ld.CIT(A) agreed with the contention of the A.O. by reasoning that the receipts/expenses are not corelatable. Ld. CIT(A) further confirmed the disallowance of certain expenditure under certain heads by adducing that the expenses are substantial, excessive, unreasonable, disproportionate, claimed for the first time and unverifiable, etc.</p>	<p>The A.O. cannot determine the level and type of functions and entertainment programmes of members, organised for the members’ benefit during the course of year. The Club is not a commercial entity seeking to jack up artificially any revenue expenditure to camouflage any taxable income. The Club is a mutual entity and its expenditure is governed by the requirements of its members in the sphere of recreational, sports, games, etc. Further, the expenditure under various heads of account incurred during the year under assessment is true, duly audited by the Statutory auditors and the said accounts have received the approval of the general Body of the Members during the Annual General Meeting.</p> <p>The reasoning advanced by A.O. and confirmed by Ld. CIT (A) by estimating lesser amount of expenditure on a presumptuous basis instead of on real expenditure basis. The reasoning that the receipts/expenses are not co-relatable is not rational and tenable by any canon of justice.</p> <p>While there was deficit under Entertainment programmes A/c. of a sum of rs.5,41,338/-, the A.O. arbitrarily estimated an income of rs.36,350/- is not acceptable. The club having more than 1000 members, incurs expenditure on Entertainment events regularly every month by way of recreational facility for its members. Bit function like New Year’s</p>

	<p>Eve Function, Christmas Eve, Diwali eve, Fashion Show, Antakshari, etc. were celebrated on a grand scale and there is no reason that the actual expenditure duly audited by the statutory auditors, is not admitted by the A.O.</p> <p>The A.O.'s arbitrary reduction of expenditure under "Entertainment programmes" on the plea that the expenditure under the head was more than last year is not acceptable under any logic. Similarly, the Id. CIT(A) grossly erred in confirming the disallowance of certain expenditure under the head "Card room. Billiards, Tennis &amp; other games" on the pleas that they are substantial, excessive, unreasonable, disproportionate, claimed for the first time and unverifiable, etc. Because, the expenditure were actuals, emanating from the events and as such the expenditure cannot be dismissed by stroke of pen by adducing that they are excessive and substantial, unverifiable, etc. The Appellate authority is wrong in agreeing with the Id. A.O. for such disallowance by reason of the fact they cannot determine the level and size of the expenses of the recreational aspects of the club with more than one thousand members. The disallowance of the expenses on the plea of excessive is fictional and is beyond jurisdiction of the A.O.</p>
<p>7. Ld. CIT(A) held by agreeing with Ld. A.O. that the "entrance fee" of Rs.12,00,000 received by the club from its members at the time seeking membership of the club, as revenue receipt (instead of capital receipt) by adducing that the concept of mutuality is not applicable in this case; and that the appellant club has not challenged the applicability of ratio of decision relied on by A.O. as in the case of United Club and Madras Race Club reported in 161 ITR 853 and 210 ITR 680 respectively. In support of his judgement,</p>	<p>Contrary to the Standard practices and accepted principles of Accounting, generally allowed by ICAI, the Ld. CIT(A) grossly erred in agreeing with A.O., that "entrance fees" received by the club to be treated as "revenue receipt" instead of "capital receipt" on the plea that the Articles of Association of the club do not specifically lay that the entry fee collected from the members shall the capital fund of the club. In fact entrance fee vests in the contributor the right of the club and assumes the nature of capital receipt in the</p>

the L.d. CIT(A) cited that “the articles of Association of the club nowhere lay that the entry fee collected from the members shall be the capital fund of the club and refundable to the members as such when the membership ceases. He maintained that the entry fee collected from members and used for providing club service to members and non-members has been correctly held as revenue receipts.

hands of the assessee-club since the club’s Articles of Association do not provide for capital base of the club. The treatment of the receipts like Entrance Fees as Revenue Receipt as professed by the Ld. CIT(A) proves specie of his prejudicial mind towards the Appellant’s case, since such contrived interpretation of the Ld. CIT(A) is much against the Accounting doctrines and practices.

Unlike in a commercial company, the liability of the club is limited by guarantee and the Articles of association of the club do not provide for separate equity capital for the reason that the club is designed for providing services and recreational facilities on the principle of mutuality. Entrance fees in the club is neither transferable (like in a commercial company) nor the same is refundable as and when the membership ceases. Entrance fees vest the right of membership for partaking in the activities of the club including that of exercising the vote in the Annual General Meeting, Based on standard practices adopted by ICAI and accounting practices followed by Chartered Accountants, the entrance fees form the General Fund (in lieu of capital) and the same becomes (lie capital receipt for creating assets for use of the members, by recourse to capital expenditure account (and not revenue account). Hence, Entrance fees are classified as General Fund for accounts purposes, under the Funds and Liabilities of the club by the Chartered Accountants, instead of Revenue Account under Profit and Loss Account. It may be stated that even if the CIT(A)’s vain attempt for compounding Capital Account Receipts under Entrance Fees paid by members with the Receipts under Revenue A/c., the taxability of such surplus created out of excess receipts over expenditure - as a result of mutuality principle of the Club,

cannot be treated as "Income" or the purpose of the IT Act. (vide supreme Court Judgement dated 8.5.97 under Civil Appeal Nos. 854 to 858 of 1984, etc. in r/o CIT vs. Bankipur club Ltd.). In fact, "Entrance Fee" paid by the Members at the time of admission (in the absence of issue of shares by the Club) vests the right of Membership in an Applicant Member, which confers inter alia the right to vote in the election of the Committee of the Club. Hence, the Entrance Fees are capitalised under a common fund viz., "General Fund" and cannot be clubbed with Revenue Income for the purpose of computing Tax liability since it is neither "Income, Profit, nor gains earned or arising, accruing to a person or body of persons".

The Ld. Appellate Authority is grossly erroneous in interpreting that the entry fees of members are refundable as and when their membership ceases. The Articles of association of the Club has no provision to either transfer the entrance fee or refund the same and when the member ceases to be member. As stated above, the Entrance Fees are capitalised under a Common Fund {"General Fund"}, which is used for creating assets for use of the members, apart from using the General Fund for netting out the Club Revenue losses or revenue surpluses, as the case may be, each year.

Regarding the revenue's comment that "entry fee collected from members and used for providing club service to members and non-members has been correctly held as revenue receipt" has already been clarified in the earlier paragraphs. Providing of Club service to Members and their guests (who may lie non-members but guests of the host members does not preclude the claim of the Club from mutuality so. long as the services provided

by the Club are paid by the host members.

The Club does not receive any payment from the guests (who may be non-members) and hence the attempt for classifying the Entry fee under Revenue receipts by the revenue is arbitrary and bears out no principle. AO's prejudice against the Club does not efface the mutuality genre of the Club. Books of Accounts of the Club are kept by the Club in accordance with the provisions of the Companies Act under section 209. The Annual Accounts and Balance Sheet are prepared in accordance with the provisions of section 210 and section 211 of the Act *ibid*. The Accounting Standards are based on the National Advisory Committee on Accounting Standards as well as norms and standards prescribed and practised by the Institute of Chartered Accountants of India. According to the standard norms and practices, the Accounts of the Club are computed and audited and certified by the Statutory Auditors with their Audit report and the same is adopted and accepted by the Annual General Meeting of the Club as per the provisions of the Companies Act. When the above process of accounting / auditing / reporting / adopting of the Accounts under the Companies Act accept the "Entry Fees/ Entrance Fees" received by the Club from the members at the time of their admission into the Club, as a receipt under the Capital Account grouped under the "General Fund" of the Club, it is not understood as to how the AO and the CIT (A) make a departure in the treatment of the "Entrance/Entry Fees" as a revenue receipt, obviously they erred with prejudice against the Club without any substance.

It is relevant to cite here the judgment of the Hon'ble Supreme Court (*Apollo Tyres vs. CIT, Kochi*) where the Apex Court clearly ruled that there cannot be two sets

of accounts; one for the purpose of Companies Act and the other for the purpose of Income Tax Act and further ruled “the Assessing Officer does not have jurisdiction to go behind ... profit & loss account except to the extent provided in Explanation 115J”. the Apex Court further clarified that “if the legislature intended the assessing officer to reassess the company’s income, then it would have stated in section 115J that the “Income of the company as accepted by the assessing officer”. Although the Apex Court’s ruling relates to the issues pertaining to assessment of income with reference to section 115J of the IT Act, the merit of the apex court’s judgment aptly applicable to the present case of the Club and the assessing officer per se has no jurisdiction to alter the audited/ certified accounts and adopted by the members of the Club in the Annual General Meeting., with a prejudicial motive for the purpose of raising Income Tax demand against the Club. Thus the treatment of Entry/Entrance Fees as revenue receipt by the AO/CIT(A) is grossly wrong in principle and practice and not is maintainable.

Incidentally, the Ld. CIT(A), after enjoying the membership of the club till end of December, 2001, made an application to the club for seeking refund of his entrance fees by resigning from the membership with the club due to his transfer to another section. Being a member of the club, and being a sitting appellate authority, trying the appeal case of the club, it speaks of his knowledge of the provisions of the Articles of Association which, of course, do not provide for refund of the entrance fees wither on resignation or otherwise. No where in the Articles of Association, there is any mention of refund of the entry fees to the members for the obvious reason that the common fund corpus under “General

	Fund” of the Club cannot be pre-empted through recourse to refunds to members, thereby causing a threat to the existence of the entry of the mutual Club.
<p>8. Ld. CIT(A) confirmed the receipt of Rs.3,00,000/- from ITC Ltd., received by the club towards construction of Wills Pub (and not the whose of it) is in the nature of revenue receipt and not capital receipt by reason that the nature of money received for advertisement as is the case with other advertisements by way of display on notice board of the club or hoardings is a revenue receipt brought to tax as such.</p>	<p>The contention of Id. CIT(A) in equating Hoardings and advertisements displayed on the Notice Board with that of the Capital asset like wills Pub is rather irrational and bereft of judicial prudence. The capital expenditure construction of Wills Pub as per the request of the ITC Ltd. was far more than Rs.3 lakhs as funded by the sponsorer and the balance amount of the capital expenditure was met by club’s capital funds. There is no reason that the capital expenditure for Wills Pub could ever have been wrongly booked as revenue receipt. Wills Pub is a physical asset and hence the relative expenditure needs to be exhibited under capital account instead of under revenue account. If the sum of Rs.3,00,000 received from ITC Ltd. for construction of Wills Pub is to be reckoned as revenue expense, there cannot remain a physical asset like Wills Pub in the club premises. The Appellate authority grossly erred in comparing the Wills Pub physical asset with that of the advertisements on notice board or in the hoardings. The relative expenditure of wills Pub may constitute as revenue expenditure for the donor (ITC Ltd.), but the same, on receipt in the hands of the club, becomes capital receipt for expenditure towards capital asset by virtue of the fact that the amount has been incurred for creating a physical/capital asset for the club.</p>
<p>9. Club’s KOT/BOT do not bear the membership number or the name of the member; on a given date the amount is debited or collected from a member does not correspond to entry in the counter/guest register.</p>	<p>The Ld. CIT(A) is wrong in his statement, KOT/UOT do bear the provision of space earmarked for the name and number of the member. The member writes his name and number in the earmarked space and accordingly the amount is debited or collected from respective members with corresponding entry made in the respective registers for enabling billing to the</p>

	<p>respective members. Even on assumption that the KOT/BOT do not bear the membership number and name of member, as wrongly adduced by the Ld. CIT(A), the matter of procedural lapse does not efface the mutuality character of the club. What is more important is the substantive issue (relevant to the appeal) as to whether the club services provided to members is brought to the records of respective members' billing for seeking settlement of payment either in cash or credit.</p>
<p>10. There is no control over receipt / processing thereof and refund of application money, if at all. Despite specific letters dated 25.9.2001 and 18.10.2001, the appellant conveniently avoided furnishing numbers P-751 and P-826 to P-875 which would have reinforced above findings and also that some persons have been arbitrarily made members on receipt of even lower than the minimum prescribed fees and some even on the out-of-run basis where applications have been processed with a jet speed even without the meeting of the Executive Committee.</p>	<p>That the conclusion Id. CIT(A) about the procedures of induction of new members adopted by the Club is not only irrelevant to the issue and also bad in law since the matter of processing applications for Membership of the club is purely an internal matter and is privy to the Management. The practice of induction of new members varies from club to club depending on the exigencies and the club reserves it right to choose its own discretionary practices as is within the propriety of the Club's Management being voted upon by the members themselves. The Ld. CIT(A) had called for certain specific application forms with a malafide intention where he had vested interests instead of anything to do with the adjudication proceedings. The comments and assumptions of the CIT(A) in the matter are uncalled for and have no relevance to the contentious issue. However, the details of receipt and processing of application forms received from applicants as called for by the Ld. CIT(A) were furnished.</p> <p>Mention may be made that the admission of members is not open through advertisement or any such process by virtue of the fact that the activities of the club are governed by the principle of mutuality. It is purely an internal matter of the Club and Club administration.</p>

Applications of persons seeking membership of the club are to be proposed and seconded by existing eligible members. The processing of such applications and time taken for their disposal as per admission procedure laid down in the Articles of Association of the club as well as Club the rules, varies from case to case depending on the circumstances, type and eligibility of the applicant and the decision of the executive Committee is final. It is totally untrue that applications for membership are finalised without the approval of the Executive Committee. It is possible that due to exigencies, some applications are considered / approved out-of-turn for which post facto approval of the Executive Committee is taken as is expedient to the case. The club maintains that the processing of applications for membership is an internal matter of the club and it has no relevance to the proceedings of the appeal for “reinforcing the finding” of the Appellate authority. Incidentally, the information called for processing of applications for admission of members by Ld. CIT(A) is neither central to the issue under appeal nor to the aspect of the taxability of the club, in general.

The findings of the Ld. CIT(A) exhibit his preconceived prejudicial motive, who (being a member of the club) held a veiled threat against club for enrolling his persons as members of the club, by keeping the disposal of the appeal pending for a long a time. Many of his persons (including a lady), proposed / seconded by him were admitted as members in the club, excepting one case in the last, during the pendency of the appeal. He subsequently, for reasons best known to him, verbally desired that membership one of members admitted at this instance should be terminated, but it was not complied with by the club for reasons of equity and justice and therefore,

	it is obvious that his issue of appellate judgement (timed with his transfer from Bhubaneswar) in the Appeal did not go in favour of the club despite sufficient reasons were to justify the stand of the club.
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10. The Id. counsel has further filed his written note to support the claim that doctrine of mutuality will apply in the present case. The same is reproduced below :

“Under the IT Act, what is the income, profits or gains earned or “arising”, “accruing” to a “person”. Where a number of persons combine together and contribute to a common fund for engaging themselves for common benefit to themselves, then any surplus returned to them cannot be regarded in any sense as profit. Where the 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 enterprise. The surplus - excess of receipts over expenditure - as a result of mutual arrangement, cannot be said to be “Income for the purpose of Income Tax Act.

According to the Articles of Association of the Club, the Membership of the Club vests the inherent right in the Members for certain the privileges which includes bringing of guests authorised for the occasion to partake in the Club facilities along with the host members and it does not amount to violation of the principle of mutuality so long as such services are paid for by the host members and not by the guests. It is a settled law that “merely because the Club even if entered into transactions with non-members and earned profits out of such transactions, the Club’s right to claim exemption on the principle of mutuality in respect of such transactions held by it with its members is not lost. The assessee was a mutual concern. The Income derived by from its house property to its members and their guests was not taxable in its hands”.(of Patna High Court vide (1992) 196 ITR 137 (Pat) : TC 38R, 576 Page 139). Even the Hon’ble Supreme Court held in the case of CIT v. The Bankipur Club Ltd. “Where the trade or activity is mutual, the fact that, as regards certain activities, certain members of the Club only take advantage of its facilities which it offers does not affect the mutuality of the enterprise”. The Revenue failed to take cognisance of the Apex Court’s view and accept the claim of the Club on mutuality principle.

Again the Hon’ble Supreme Court of India (in the case of Chelmsford Club vs. CIT - (2000) 159 CTR (SC) 235) held further *that even deemed income from property of the Club is also outside the purview of levy of income-tax*. The Apex Court contended that *the Club’s business is governed by the principle of mutuality, which, in turn, is based on a*

*doctrine that no person can earn from himself. Every member pays for his own expenses and there is no profit motivation or sharing of profits as such amongst the members. The surplus, if any, from the business is not shared by members but is used for providing better facilities to the members. No outsider is allowed to take part and the facilities provided by the appellant Club is exclusively for its members and their guests. Therefore, there is a clear identity between the contributors and the participators to the common fund and the recipients thereof respectively.*

Hiring out of Club lawns to the Members for holding parties (alleged as “large”) on the occasions of wedding, other functions, etc., whereas the guests of host-members (being non-members who also partake the facilities) cannot be construed as a violation of the principle of mutuality by the Club on the plea that members’ parties should not be large and should be limited to “ordinary limited guests”. It should be recognised of the fact that the Club has provided services only to the host members and at host-members’ request the guests of host members partook the Club services and as such the Club has not violated its mutuality principle. Bereft of the above, even if any, surplus accrued to the Club upon such services made to host members along with their guests, cannot be regarded as an income for the fact that the so called surplus flows into the common fund (general Fund) only to sub-serve the interest of the members for furthering the common amenities of the Club. Hence such surplus is not exigible to income-tax at any rate.”

11. We have heard both the sides at length and considered the written submissions from both the sides, its replies and comments by the assessee. We have gone carefully the entire materials placed on record. We have also perused the order of the Hon’ble Supreme Court in the case of Bankipur Club Ltd. (supra) on which both the sides have placed reliance. On careful consideration of the Assessing Officer’s order we find that the Assessing Officer has proceeded to disallow the claim of mutuality i.e. the Club is a mutual concern on the basis of following reasons :-

- i) The assessee-Club has claimed its income exempt in the concept of mutuality for the first time, never before such claim was made.*
- ii) Secondly, assessee-Club has not maintained its books of account properly.*
- iii) Thirdly, that the facility of Bhubaneswar Club was not restricted only to the members but non-members and outsiders have access to its benefits, services and privileges.*
- iv) Fourthly, that the members of affiliated Clubs are also entitled to the benefit, services and privileges of the Club.*
- v) Fifthly, guest room facilities which are its substantial sources of earning, are available to both members, non-members and their guests and affiliated Clubs.*

Before coming to various reasons given by the Ld. Counsel to deny the claim of exemption of income on the principle of mutuality, it is considered necessary to discuss the principle of mutuality. Hon'ble Andhra Pradesh High Court in the case of CIT vs. Merchant Navy Club (1974) 96 ITR 261 (AP) after reviewing and discussing the leading cases on the subject has summarised the principle of mutuality as under :-

“No person can trade with himself and make an assessable profit. If instead of one person more than one combine themselves into a distinct and separate legal entity for the purpose of rendering services to themselves or for the supply of refreshments, beverages, entertainment, etc., by over-charging themselves, the resulting surplus is not assessable to tax if the surplus is to be refunded to the members. The contributors to the common fund and the participators in the surplus must be an identical body. That does not mean that each member should contribute to the common fund or that each member should participate in the surplus or get back from the surplus precisely what he has paid. What is required is that the members as a class should contribute to the common fund and participators as a class must be able to participate in the surplus. It is immaterial whether the surplus is paid back to the members in cash or is put to reserve with the club for its development and for providing better amenities to its members. When the body of individuals is incorporated into a company or formed into a registered society, what is essential is that it should not have dealings with an outside body which result in surplus. The participation of the members in the surplus must be in their character as contributors to the common fund or as consumers, and not as shareholders getting dividends on their share amount or as debenture-holders earning interest. In all cases of incorporation as a company or as a registered society, the proper mode of regarding the company or the registered society is that it is a convenient instrument or medium for enabling the members to conduct a social club, the objects of which are immune from every taint of commerciality. The property of the incorporated company or a registered society, for all practical purposes in this behalf, is considered as property of the members. A members club formed for social intercourse and for either recreation or cultural activities cannot be considered to trade for profit so as to make its surplus taxable in law when it over-charges its members for the supply of refreshments, beverages or amenities to its members. Such supplies are not sales as there is no element of transfer of property in them.”

The above principle of mutuality was taken into consideration by the Hon'ble Patna High Court (FB) while deciding the case of CIT vs. Ranchi Club Ltd. (1992) 196 ITR 137 (Pat.). Keeping in view the above observations of Hon'ble Andhra Pradesh High Court and the observations of the Hon'ble Supreme Court in the case of Bankipur Club Ltd., we shall proceed to decide the issue before us.

11.1 The first ground taken by the Assessing Officer to deny the claim of the assessee that such claim was never made before. We find that this observation of the Assessing Officer has been fully replied in its written submission. The sum and substance of which are that, in past, such occasion never arose and it is only first time that the issue was raised by the Assessing Officer consequently, the assessee had to claim in black and while that the Club was a mutual concern and its income was not subjected to tax. We are in full agreement with the reply of the assessee on this ground.

11.2 The second ground taken by the Assessing Officer that the books of accounts were not properly maintained is also of not much importance for the purpose of deciding whether the Club is a mutual concern though the Club has properly maintained books of accounts and no serious defects have been pointed out in the maintenance of books of accounts. There may be lapses here and there but there was no such serious defects which may lead to rejection of books of accounts and that cannot be a valid ground for claiming that the income of the assessee is not exempted as because Club is a mutual concern. Now, coming to the enjoyment facility benefit services and privileges of the Club by the alleged non-members, we find that the authorities below have a wrong notion about the use of Club by the non-members. The facilities of the Club are used only by the members or their relatives or by their guests. No person can even enter into the premises of the Club without the recommendation of the member. It is only the member who takes their relatives or guests to the Club. The revenue has again and again referred to the decision of Hon'ble Supreme Court in the case of Bankipur Club Ltd., where it has been held that if the Club is used by non-members, it cannot be said that Club is a mutual concern but the question whether "non-member" occurring in the decision of Hon'ble Supreme Court also includes relatives of the members, guests of the members and the members of affiliated Clubs. Our plain and simple answer is that the relatives, guests of the members and members of affiliated Clubs do not fall in the category of "non-member". This view of ours have been derived from the decision of Hon'ble Supreme Court in the case of Bankipur Club Ltd. itself. When the decision of Hon'ble Supreme Court was taken in the case of Bankipur Club Ltd., it was not only the issue involved in the case of Bankipur Club Ltd., but the issue involved in other three Clubs were also decided and three other Clubs are - Ranchi Club Ltd., Cricket Club of India & Northern India Motion Picture Association. The question refers to Hon'ble High Court in the case of Ranchi Club Ltd. Reported in (1992)196 ITR 137 (Pat.) (FB) was as under :-

- (i) *Whether, on the facts and in the circumstances of the case, the Tribunal has rightly held that the assessee-club is a 'mutual concern'?*
- (ii) *Whether, on the facts and in the circumstances of the case, the Tribunal has rightly held that the income derived by the assessee-club from its house property let to its members and their guests is not chargeable to tax? (emphasis supplied)*
- (iii) *Whether, on the facts and in the circumstances of the case, the Tribunal has rightly held that the income derived by the assessee-club from sale of liquor, etc., to its members and their guests is not*

*taxable in its hands? (emphasis supplied)*

On perusal of the above questions referred to Hon'ble Patna High Court (FB) will show that the second & third question are the same which are involved in the present case and these questions have been answered by Hon'ble High Court in favour of the assessee and the same has been endorsed by the Hon'ble Supreme Court. Thus, it is quite clear that when the Hon'ble Supreme Court decided the case it was very much aware that Ranchi Club Ltd. was deriving income from its house property which let to the members and their guests which was held not to be taxable. Thus, in our considered opinion, the concept of "member" is spacious enough to include guests and relatives of the members and members of affiliated Clubs, and if it is so, then in the case of appellant the income derived by letting out its premises or by allowing the guests and relatives of the members and members of affiliated Clubs will not be subjected to tax. Thus, in our considered opinion, services offered to the guests, relatives and affiliated Clubs cannot be treated as trading activity, therefore, cannot be tainted with commerciality. Accordingly, we hold that the appellant-Club is a mutual Club and the various activities highlighted by the authorities below cannot be put in the category of trading activity or in the category of adventure in the nature of trade, hence, not taxable.

12 Since we have held that the entire receipts of the Club are exempt from tax, the grounds in cross appeal by the revenue becomes infructuous, hence, dismissed.

13. As a result, assessee's appeal is allowed and the revenue appeal is dismissed.

Orders pronounced in the open Court on 29/8/06

(N.L. Dash)  
Judicial Member

(R.P. Rajesh)  
Accountant Member

Dated : 29th August, 2006.

Copy of the order is forwarded to :-

- 1) Bhubaneswar Club Limited, Rajpath Road, AG Square, Bhubaneswar.
- 2) Asstt. Commissioner of Income Tax, Circle-1(1), Bhubaneswar.
- 3) CIT(A)- (4) CIT-
- 4) A. R., I.T.A.T., Cuttack

(True Copy)

By Order

*[Handwritten Signature]*  
for Assistant Registrar

I.T.A.T.,

Cuttack  
(KKC)