M/S. Bangalore Club vs Commissioner Of Income Tax & Anr on 14 January, 2013

Equivalent citations: 2013 AIR SCW 545, 2013 (1) AKR 522, AIR 2013 SC (SUPP) 851, (2013) 124 ALLINDCAS 4 (SC), (2013) 4 KCCR 393, (2013) 1 CURCC 98, (2013) 1 SCALE 365, 2013 (5) SCC 509, (2013) 350 ITR 509

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Bench: D.K. Jain, Jagdish Singh Khehar

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      |IN THE SUPREME COURT OF INDIA                                 |
      |CIVIL APPELLATE JURISDICTION                                  |
      |CIVIL APPEAL  NO. 124 OF 2007                                 |
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      |M/S. BANGALORE CLUB              |—         |APPELLANT        |
      |VERSUS                                                        |
      |COMMISSIONER OF INCOME TAX & ANR.  |—       |RESPONDENTS      |
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WITH

CIVIL APPEAL NO. 125 OF 2007,

CIVIL APPEAL NO. 272 OF 2013
(Arising out of S.L.P.(Civil) No. 16863 of 2010),

CIVIL APPEAL NO.273 OF 2013
(Arising out of S.L.P.(Civil) No. 16880 of 2010),

CIVIL APPEAL NO.274 OF 2013
(Arising out of S.L.P.(Civil) No. 16881 of 2010),

CIVIL APPEAL NO.275 OF 2013
(Arising out of S.L.P.(Civil) No. 16882 of 2010)

CIVIL APPEAL NOS.276-277 OF 2013
(Arising out of S.L.P.(Civil) Nos. 16883-16884 of 2010)

AND

CIVIL APPEAL NO.278 OF 2013
(Arising out of S.L.P.(Civil) No. 16879 of 2010)

J U D G M E N T

D.K. JAIN, J.

1. Leave granted in Special Leave Petitions.

2. This batch of appeals arises from a common judgment and order pronounced by the High Court of Karnataka, in Income Tax Appeals No. 115 of 1999 along with 70 of 2000, 3095 of 2005, 1547 of 2005, 1548 of 2005, 3091 of 2005, 3089 of 2005 along with 3093 of 2005, and 3088 of 2005. Since these appeals entail the same issue, they are being disposed of by this common judgment.

3. The facts necessary for the purpose of appreciating the controversy involved in the appeal are as follows:

> The Bangalore Club (hereinafter referred to as the "assessee"), the appellant herein, is an unincorporated Association of Persons, (AOP). In relation to the assessment years 1989-90, 1990-91, 1993-94, 1994-95, 1995- 96, 1996-97, 1997-98, 1998-99 and 1999-2000, the assessee sought an exemption from payment of income tax on the interest earned on the fixed deposits kept with certain banks, which were corporate members of the assessee, on the basis of doctrine of mutuality. However, tax was paid on the interest earned on fixed deposits kept with non-member banks.
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> The assessing officer rejected the assessee's claim, holding that there was a lack of identity between the contributors and the participators to the fund, and hence treated the amount received by it as interest as taxable business income. On appeal by the assessee, the Commissioner of Income Tax (Appeals)-II, Bangalore ("CIT (A)" for short) reversed the view taken by the assessing officer, and held that the doctrine of mutuality clearly applied to the assessee's case. On appeal by the revenue the Income- Tax Appellate Tribunal (for short "the Tribunal"), affirmed the view taken by the CIT (A), observing thus (ITA No. 2440/Ban/1991):
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> "7. In the instant case, the funds of the club are given in the form of deposits for earning income from the corporate members, namely, the banks here and, therefore, the earning of interest is clearly had risen out of the concept of mutuality only. The decisions relied upon by the DR have nowhere touch (sic) upon the fact as to whether it was with corporate members or not. Apparently, they had dealt with the situation where the transactions of interest are from persons who are not the members of the club. During the argument, the DR had admitted that the assessee had shown interest from certain other banks as its income which also goes to show that wherever the concept of mutuality was absent, the assessee had offered the same as income." On an application by the Commissioner of Income Tax, Bangalore under Section 260A of

the Income Tax Act, 1961 (for short "the Act"), the High Court entertained the appeal and framed the following two substantial questions of law for its adjudication :-

"(1) Whether, a sum of Rs. 7,87,648/- received by the assessee as interest from fixed deposit made by the assessee in four banks who are members in the assessee club amounted to its income and constituted a revenue receipt as per the provision of Income Tax Act.

(2) Whether, the principle of mutuality can be made applicable to the fund deposited in the four banks who are also members of assessee club, especially when the fund is raised from contribution of several members including the four banks and the interest derived from it is utilized by several members of the assessee club?" Answering both the questions in favour of the revenue, the High Court held :-

"12. On the facts of this case and in the light of the legal principles it is clear to us that what has been done by the club is nothing but what could have been done by a customer of a Bank . The principle of 'no man can trade with himself' is not available in respect of a nationalised bank holding a fixed deposit on behalf of its customer. The relationship is one of a banker and a customer." Consequently, the High Court reversed the decision of the Tribunal and restored the order of the assessing officer. Hence, this appeal by the assessee.

4. Thus, the short question for determination is whether or not the interest earned by the assessee on the surplus funds invested in fixed deposits with the corporate member banks is exempt from levy of Income Tax, based on the doctrine of mutuality?

5. Mr. Joseph Vellapally, learned senior counsel appearing for the assessee strenuously urged that the assessee meets all the requirements, as laid down in The English & Scottish Joint Co-operative Wholesale Society Ltd. Vs. The Commissioner of Agricultural Income Tax, Assam[1], as affirmed by this Court in Chelmsford Club Vs. Commissioner of Income Tax, Delhi[2] in order to fall within the ambit of the principle of mutuality. According to the learned counsel, there is a complete identity between the contributors to the fund and the assessee and the recipients from the funds, in as much as the interest earned by the assessee from the surplus fund invested in fixed deposits with member banks are always available and are used for the benefit of members alike. It was asserted that there is no commercial motive involved in the dealings of the assessee with its members, including the banks concerned. It was also argued that the interest earned on such deposits with the member banks was always available for use and benefit of the members of the assessee, in as much as the said interest merged with the common fund of the club.

6. Mr. A.S. Chandhiok, learned Additional Solicitor General of India, on the other hand, contended that the fundamental principle for applicability of the doctrine of mutuality is a complete identity between the contributors and the participators, which is missing in this case. It was submitted that in the present case, the surplus funds in the hands of the assessee were placed at the disposal of the corporate members viz. the banks, with the sole motive to earn interest, which brings in the

commerciality element and thus, the interest so earned by the assessee has to be treated as a revenue receipt, exigible to tax. It was pleaded that transaction between the assessee and the member banks concerned was in the nature of parking of funds by the assessee with a corporate member and was nothing but what could have been done by a customer of a bank and therefore, the principle that "no man could trade with himself" is not applicable.

7. Before we evaluate the rival stands, it would be necessary to appreciate the general understanding of doctrine of mutuality. The principle relates to the notion that a person cannot make a profit from himself. An amount received from oneself is not regarded as income and is therefore not subject to tax; only the income which comes within the definition of Section 2(24) of the Act is subject to tax (income from business involving the doctrine of mutuality is denied exemption only in special cases covered under clause (vii) of Section 2 (24) of the Act). The concept of mutuality has been extended to defined groups of people who contribute to a common fund, controlled by the group, for a common benefit. Any amount surplus to that needed to pursue the common purpose is said to be simply an increase of the common fund and as such neither considered income nor taxable. Over time, groups which have been considered to have mutual income have included corporate bodies, clubs, friendly societies, credit unions, automobile associations, insurance companies and finance organizations. Mutuality is not a form of organization, even if the participants are often called members. Any organization can have mutual activities. A common feature of mutual organizations in general and of licensed clubs in particular, is that participants usually do not have property rights to their share in the common fund, nor can they sell their share. And when they cease to be members, they lose their right to participate without receiving a financial benefit from the surrender of their membership. A further feature of licensed clubs is that there are both membership fees and, where prices charged for club services are greater than their cost, additional contributions. It is these kinds of prices and/or additional contributions which constitute mutual income.

8. The doctrine of mutuality finds its origin in common law. One of the earliest modern judicial statements of the mutuality principle is by Lord Watson in the House of Lords, in 1889, in Styles (Surveyor of Taxes) Vs. New York Life Insurance Co.[3] (hereinafter referred to as the "Styles case"). The appellant in that case was an incorporated company. The company issued life policies of two kinds, namely, participating and non- participating. The members of the mutual life insurance company were confined to the holders of the participating policies, and each year, the surplus of receipts over expenses and estimated liabilities was divided among them, either in the form of a reduction of future premiums or of a reversionary addition to the policies. There were no shares or shareholders in the ordinary sense of the term but each and every holder of a participating policy became ipso facto a member of the company and as such became entitled to a share in the assets and liable for a share in the losses. The company conducted a calculation of the probable death rate amongst the members and the probable expenses and liabilities; calls in the shape of premiums were made on the members accordingly. An account used to be taken annually and the greater part of the surplus of such premiums, over the expenditure referable to such policies, was returned to the members i.e. (holders of participating policies) and the balance was carried forward as a fund in hand to the credit of the general body of members. The question was whether the surplus returned to the members was liable to be assessed to income tax as profits or gains. The majority of the Law Lords answered the question in the negative. It may be noticed that in that case the members had

associated themselves together for the purpose of insuring each other's life on the principle of mutual assurance, that is to say, they contributed annually to a common fund out of which payments were to be made, in the event of death, to the representatives of the deceased members. Those persons were alone the owners of the common fund and they alone were entitled to participate in the surplus. This surplus was obtained partly from the profits arising from non-participating policies and other business. It was held that that portion of the surplus which arose from the excess contributions of the holders of participating policies was not an assessable profit. It was therefore, held to be a case of mutual assurance. The individuals insured and those associated for the purpose of receiving their dividends and meeting other stipulated requisites under the policies were identical. It was held that that identity was not destroyed by the incorporation of the company. Lord Watson even went to the extent of saying that the company in that case did not carry on any business at all, which perhaps was stating the position a little too widely as pointed out by Viscount Cave in a later case; but, be that as it may, all the Noble Lords, who formed the majority, were of the view that what the members received were not profits but their respective shares of the excess amount contributed by themselves. They held thus:

> "... when a number of individuals agree to contribute funds for a common purpose ... and stipulate that their contributions, so far as not required for that purpose, shall be repaid to them. I cannot conceive why they should be regarded as traders, or why contributions returned to them should be regarded as profits."

9. Lord Watson's statement was explained by the House of Lords in The Commissioners Of Inland Revenue Vs. The Cornish Mutual Assurance Co. Ltd.[4] wherein it was held that a mutual concern may be held to carry on a business or trade with its members, though the surplus arising from such trade is not taxable income or profit.

10. The High Court of Australia first considered the mutuality principle in The Bohemians Club Vs. The Acting Federal Commissioner of Taxation[5] in 1918:

> "A man is not the source of his own income ... A man's income consists of moneys derived from sources outside of himself. Contributions made by a person for expenditure in his business or otherwise for his own benefit cannot be regarded as his income ... The contributions are, in substance, advances of capital for a common purpose, which are expected to be exhausted during the year for which they are paid. They are not income of the collective body of members any more than the calls paid by members of a company upon their shares are income of the company. If anything is left unexpended it is not income or profits, but savings, which the members may claim to have returned to them." (Emphasis added)

11. One of the first Indian cases that dealt with the principle was Commissioner of Income-Tax, Bombay City Vs. Royal Western India Turf Club Ltd.[6]. It quoted with approval three conditions stipulated in The English & Scottish Joint Co-operative Wholesale Society Ltd. (supra), which were propounded after referring to various passages from the speeches of the different Law Lords in Styles case (supra). Lord Normand, who delivered the judgment of the Board summarized the

grounds of the decision in Styles case (supra) as follows:

> "From these quotations it appears that the exemption was based on (1) the identity of the contributors to the fund and the recipients from the fund; (2) the treatment of the company, though incorporated, as a mere entity for the convenience of the members and policy holders, in other words, as an instrument obedient to their mandate; and (3) the impossibility that contributors should derive profits from contributions made by themselves to a fund which could only be expended or returned to themselves."

12. We will consider each of these conditions in detail before proceeding to the facts of the case. The first condition requires that there must be a complete identity between the contributors and participators. This was first laid down by Lord Macmillan in Municipal Mutual Insurance Ltd. Vs. Hills[7] wherein he observed:

> "The cardinal requirement is that all the contributors to the common fund must be entitled to participate in the surplus and that all the participators in the surplus must be contributors to the common fund; in other words, there must be complete identity between the contributors and the participators."

13. On this aspect of the doctrine, especially with regard to the non- members, Halsbury's Laws of England, 4th Edition, Reissue, Vol. 23, paras 161 and 162 (pp. 130 and 132) states:

> "Where the trade or activity is mutual, the fact that, as regards certain activities, certain members only of the association take advantage of the facilities which it offers does not affect the mutuality of the enterprise.
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> * * * Members' clubs are an example of a mutual undertaking; but, where a club extends facilities to non-members, to that extent the element of mutuality is wanting...."
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> 14. Simon's Taxes, Vol. B, 3rd Edn., paras B1.218 and B1. 222 (pp. 159 and
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> 167) formulate the law on the point, thus:
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> "..it is settled law that if the persons carrying on a 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. Any surplus resulting from this form of trading represents only the extent to which the contributions of the participators have proved to be in excess of requirements. Such a surplus is regarded as their own money and returnable to them. In order that this exempting element of mutuality should exist it is essential that the profits should be capable of coming back at some time and in some form to the persons to whom the goods were sold or the services rendered....

* * * It has been held that a company conducting a members' (and not a proprietary) club, the members of the company and of the club being identical, was not carrying on a trade or business or undertaking of a similar character for purposes of the former corporation profits tax.

* * * A members' club is assessable, however, in respect of profits derived from affording its facilities to non-members. Thus, in Carlisle and Silloth Golf Club v. Smith, (1913) 3 K.B. 75, where a members' golf club admitted non-members to play on payment of green fees it was held that it was carrying on a business which could be isolated and defined, and the profit of which was assessable to income tax. But there is no liability in respect of profits made from members who avail themselves of the facilities provided for members." (Emphasis supplied)

15. In short, there has to be a complete identity between the class of participators and class of contributors; the particular label or form by which the mutual association is known is of no consequence. Kanga & Palkhivala explain this concept in "The Law and Practice of Income Tax" (8th Edn. Vol. I, 1990) at p. 113 as follows:

"...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." The Madras, Andhra Pradesh and Kerala High Courts have held that the test of mutuality does not require that the contributors to the common fund should willy-nilly distribute the surplus amongst themselves : it is enough if they have a right of disposal over the surplus, and in exercise of that right they may agree that on winding up the surplus will be transferred to a similar association or used for some charitable objects...." (Emphasis supplied)

16. British Tax Encyclopedia (I), 1962 Edn. (edited by G.S.A. Wheatcroft) at pp. 1201, dealing with "mutual trading operations", the law is stated as under:

"For this doctrine 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, so that there is complete identity between contributors and participators. This means identity as a class, so that at any given moment of time the persons who are contributing are identical with the persons entitled to participate; it does not matter that the class may be diminished by persons going out of the scheme or increased by others coming in...." (Emphasis supplied)

17. In Jones Vs. South-West Lancashire Coal Owners' Association Ltd.[8], Viscount Cave LC held that "sooner or later, in meal or in malt, the whole of the associations" receipts must go back to the policy holders as a class, though not precisely in the proportions in which they have contributed to them and the association does not in

any true sense make any profit out of their contributions.

18. Therefore, in the case of Royal Western India Turf Club Ltd. (supra), since the club realized money from both members and non- members, in lieu of the same services rendered in the course of the same business, the exemption of mutuality could not be granted. This Court held thus:

"As already stated, in the instant case there is no mutual dealing between the members inter se and no putting up of a common fund for discharging the common obligations to each other undertaken by the contributors for their mutual benefit. On the contrary, we have here an incorporated company authorised to carry on an ordinary business of a race course company and that of licensed victuallers and refreshment purveyors and in fact carrying on such a business. There is no dispute that the dealings of the company with non- members take place in the ordinary course of business carried on with a view to earning profits as in any other commercial concern." (Emphasis supplied)

19. The second feature demands that the actions of the participators and contributors must be in furtherance of the mandate of the association. In the case of a club, it would be necessary to show that steps are taken in furtherance of activities that benefit the club, and in turn its members.

Therefore, in Chelmsford Club (supra), since the appellant provided recreational facilities exclusively to its members and their guests on "no-profit-no-loss" basis and surplus, if any, was used solely for maintenance and development of the club, the Court allowed the exception of mutuality.

20. The mandate of the club is a question of fact and can be determined from the memorandum or articles of association, rules of membership, rules of the organization, etc. However, the mandate must not be construed myopically. While in some situations, the benefits may be evident directly in the short-run, in others, they may be accruable to an organization indirectly, in the long-run. Space must be made for both such forms of interactions between the organization and its members. Therefore, as Finlay J. observed in National Association of Local Government Officers Vs. Watkins[9], where member of a club orders dinner and consumes it, there is no sale to him. At the same time, as in case of Commissioner of Income Tax, Bihar Vs. Bankipur Club Ltd.[10], where a club makes 'surplus receipts' from the subscriptions and charges for the various conveniences paid by members, even though there is no direct benefit of the receipts to the customers, the fact that they will eventually be used in furtherance of the services of the club must be considered as a furtherance of the mandate of the club.

21. Thirdly, there must be no scope of profiteering by the contributors from a fund made by them which could only be expended or returned to themselves. The locus classicus pronouncement comes from Rowlatt, J's observations in Thomas Vs. Richard Evans & Co. Ltd.[11] wherein, while interpreting Styles case (supra), he held that if profits are distributed to shareholders as shareholders, the principle of mutuality is not satisfied. He observed thus:

> "But a company can make a profit out of its members as customers, although its range of customers is limited to its shareholders. If a railway company makes a profit by carrying its shareholders, or if a trading company, by trading with the shareholders - even if it limited to trading with them - makes a profit, that profit belongs to the shareholders, in a sense, but it belongs to them qua shareholders. It does not come back to them as purchasers or customers. It comes back to them as shareholders, upon their shares. Where all that a company does is to collect money from a certain number of people - it does not matter whether they are called members of the company, or participating policy holders - and apply it for the benefit of those same people, not as shareholders in the company, but as the people who subscribed it, then, as I understand the New York case, 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 entity of the company is to be disregarded, it is because there is no profit, the money being simply collected from those people and handed back to them, not in the character of shareholders, but in the character of those who have paid it. That, as I understand it, is the effect of the decision in the New York case."

(Emphasis supplied)

22. In Commissioner of Income Tax, Madras Vs. Kumbakonam Mutual Benefit Fund Ltd.[12], this Court differentiated the facts of the case before it from those of Styles case (supra) and denied the exemption of mutuality because of the taint of commerciality. It was observed thus:

> “It seems to us that it is difficult to hold that Style's case applies to the facts of the case. A shareholder in the assessee company is entitled to participate in the profits without contributing to the funds of the company by taking loans. He is entitled to receive his dividend as long as he holds a share. He has not to fulfil any other condition. His position is in no way different from a shareholder in a banking company, limited by shares. Indeed, the position of the assessee is no different from an ordinary bank except that it lends money to and receives deposits from its shareholders. This does not by itself make its income any the less income from business within S. 10 of the Indian Income Tax Act.”

23. However, at what point mutuality ends and commerciality begins is a difficult question of fact. It is best summarized in Bankipur Club (supra) wherein this Court echoed the following views:

> “...if the object of the assessee company claiming to be a "mutual concern" or "club", is to carry on a particular business and money is realised both from the members and from non-members, for the same consideration by giving the same or similar facilities to all alike in respect of the one and the same business carried on by it, the dealings as a whole disclose the same profit earning motive and are alike tainted with commerciality. In other words, the activity carried on by the assessee in such cases,

> claiming to be a "mutual concern" or "members' club" is a trade or an adventure in the nature of trade and the transactions entered into with the members or non-members alike is a trade/business/transaction and the resultant surplus is certainly profit - income liable to tax. We should also state, that "at what point, does the relationship of mutuality end and that of trading begin" is a difficult and vexed question. A host of factors may have to be considered to arrive at a conclusion. "Whether or not the persons dealing with each other, is a 'mutual club' or carrying on a trading activity or an adventure in the nature of trade", is largely a question of fact [Wilcock's case - 9 Tax Cases 111, (p.132); C.A. (1925) (1) KB 30 at p. 44 and 45]."

24. In Royal Western India Turf Club Ltd. (supra), this Court made similar observations, holding that it is not always the case that a legal entity cannot make profits out of its members. It held as follows :

> "14...The principle that no one can make a profit out of himself is true enough but may in its application easily lead to confusion. There is nothing 'per se' to prevent a company from making a profit out of its own members. Thus a railway company which earns profits by carrying passengers may also make a profit by carrying its shareholders or a trading company may make a profit out of its trading with its members besides the profit it makes from the general public which deals with it but that profit belongs to the members as shareholders and does not come back to them as persons who had contributed them.
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> Where a company collects money from its members and applies it for their benefit not as shareholders but as persons who put up the fund the company makes no profit. In such cases where there is identity in the character of those who contribute and of those who participate in the surplus, the fact of incorporation may be immaterial and the incorporated company may well be regarded as a mere instrument, a convenient agent for carrying out what the members might more laboriously do for themselves. But it cannot be said that incorporation which brings into being a legal entity separate from its constituent members is to be disregarded always and that the legal entity can never make a profit out of its own members..." (Emphasis supplied)

25. This brings us to the facts of the present case. As aforesaid, the assessee is an AOP. The concerned banks are all corporate members of the club. The interest earned from fixed deposits kept with non- member banks was offered for taxation and the tax due was paid. Therefore, we are required to examine the case of the assessee, in relation to the interest earned on fixed deposits with the member banks, on the touchstone of the three cumulative conditions, enumerated above.

26. Firstly, the arrangement lacks a complete identity between the contributors and participators. Till the stage of generation of surplus funds, the setup resembled that of a mutuality; the flow of money, to and fro, was maintained within the closed circuit formed by the banks and the club, and to that extent, nobody who was not privy to this mutuality, benefited from the arrangement.

However, as soon as these funds were placed in fixed deposits with banks, the closed flow of funds between the banks and the club suffered from deflections due to exposure to commercial banking operations. During the course of their banking business, the member banks used such deposits to advance loans to their clients. Hence, in the present case, with the funds of the mutuality, member banks engaged in commercial operations with third parties outside of the mutuality, rupturing the 'privity of mutuality', and consequently, violating the one to one identity between the contributors and participators as mandated by the first condition. Thus, in the case before us the first condition for a claim of mutuality is not satisfied.

27. As aforesaid, the second condition demands that to claim an exemption from tax on the principle of mutuality, treatment of the excess funds must be in furtherance of the object of the club, which is not the case here. In the instant case, the surplus funds were not used for any specific service, infrastructure, maintenance or for any other direct benefit for the member of the club. These were taken out of mutuality when the member banks placed the same at the disposal of third parties, thus, initiating an independent contract between the bank and the clients of the bank, a third party, not privy to the mutuality. This contract lacked the degree of proximity between the club and its member, which may in a distant and indirect way benefit the club, nonetheless, it cannot be categorized as an activity of the club in pursuit of its objectives. It needs little emphasis that the second condition postulates a direct step with direct benefits to the functioning of the club. For the sake of argument, one may draw remote connections with the most brazen commercial activities to a club's functioning. However, such is not the design of the second condition. Therefore, it stands violated.

28. The facts at hand also fail to satisfy the third condition of the mutuality principle i.e. the impossibility that contributors should derive profits from contributions made by themselves to a fund which could only be expended or returned to themselves. This principle requires that the funds must be returned to the contributors as well as expended solely on the contributors. True, that in the present case, the funds do return to the club. However, before that, they are expended on non-members i.e. the clients of the bank. Banks generate revenue by paying a lower rate of interest to club-assessee, that makes deposits with them, and then loan out the deposited amounts at a higher rate of interest to third parties. This loaning out of funds of the club by banks to outsiders for commercial reasons, in our opinion, snaps the link of mutuality and thus, breaches the third condition.

29. There is nothing on record which shows that the banks made separate and special provisions for the funds that came from the club, or that they did not loan them out. Therefore, clearly, the club did not give, or get, the treatment a club gets from its members; the interaction between them clearly reflected one between a bank and its client. This directly contravenes the third condition as elucidated in Styles and Kumbakonam Mutual Benefit Fund Ltd. cases (supra). Rowlatt J., in our opinion, correctly points out that if profits are distributed to shareholders as shareholders, the principle of mutuality is not satisfied. In Thomas Vs. Richard Evans & Co. (supra), at pp. 822-823, he observed thus :

> "But a company can make a profit out of its members as customers, although its range of customers is limited to its shareholders. If a railway company makes a profit by carrying its shareholders, or if a trading company, by trading with the shareholders - even if it limited to trading with them - makes a profit, that profit belongs to the shareholders, in a sense, but it belongs to them qua shareholders. It does not come back to them as purchasers or customers. It comes back to them as shareholders, upon their shares. Where all that a company does is to collect money from a certain number of people - it does not matter whether they are called members of the company, or participating policy holders - and apply it for the benefit of those same people, not as shareholders in the company, but as the people who subscribed it, then, as I understand the New York case, 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 entity of the company is to be disregarded, it is because there is no profit, the money being simply collected from those people and handed back to them, not in the character of shareholders, but in the character of those who have paid it. That, as I understand it, is the effect of the decision in the New York case."

(Emphasis supplied) In the present case, the interest accrues on the surplus deposited by the club like in the case of any other deposit made by an account holder with the bank.

30. An almost similar issue arose in Kumbakonam Mutual Benefit Fund Ltd. case (supra). The facts in that case were that the assessee, namely, Kumbakonam Mutual Benefit Fund Ltd., was an incorporated company limited by shares. Since 1938, the nominal capital of the assessee was Rs.33,00,000/- divided into shares of Rs.1/- each. It carried on banking business restricted to its shareholders, i.e., the shareholders were entitled to participate in its various recurring deposit schemes or obtain loans on security. Recurring deposits were obtained from members for fixed amounts to be contributed monthly by them for a fixed number of months as stipulated at the end of which a fixed amount was returned to them according to published tables. The amount so returned, covered the compound interest of the period. These recurring deposits constituted the main source of funds of the assessee for advancing loans. Such loans were restricted only to members who had, however, to offer substantial security therefor, by way of either the paid up value of their recurring deposits, if any, or immovable properties within a particular district. Out of the interest realised by the assessee on the loans which constituted its main income, interest on the recurring deposits aforesaid was paid as also all the other outgoings and expenses of management and the balance amount was divided among the members pro rata according to their share-holdings after making provision for reserves, etc., as required by the Memorandum or Articles aforesaid. It was not necessary for the shareholders, who were entitled to participate in the profits to either take loans or make recurring deposits.

31. On these facts, as already noted, the Court distinguished Styles case (supra) and opined that the position of the assessee was no different from an ordinary bank except that it lent money and received deposits from its shareholders. This did not by itself make its income any less income from

business. In our opinion, the ratio of the said decision is on all fours to the facts at hand. The interest earned by the assessee even from the member banks on the surplus funds deposited with them had the taint of commerciality, fatal to the principle of mutuality.

32. We may add that the assessee is already availing the benefit of the doctrine of mutuality in respect of the surplus amount received as contributions or price for some of the facilities availed by its members, before it is deposited with the bank. This surplus amount was not treated as income; since it was the residue of the collections left behind with the club. A façade of a club cannot be constructed over commercial transactions to avoid liability to tax. Such setups cannot be permitted to claim double benefit of mutuality. We feel that the present case is a clear instance of what this Court had cautioned against in Bankipur Club (supra), when it said:

> "... if the object of the assessee company claiming to be a "mutual concern" or "club", is to carry on a particular business and money is realised both from the members and from non- members, for the same consideration by giving the same or similar facilities to all alike in respect of the one and the same business carried on by it, the dealings as a whole disclose the same profit earning motive and are alike tainted with commerciality. In other words, the activity carried on by the assessee in such cases, claiming to be a "mutual concern" or Members' club" is a trade or an adventure in the nature of trade and the transactions entered into with the members or non- members alike is a trade/business/transaction and the resultant surplus is certainly profit - income liable to tax. We should also state, that "at what point, does the relationship of mutuality end and that of trading begin" is a difficult and vexed question. A host of factors may have to be considered to arrive at a conclusion. "Whether or not the persons dealing with each other, is a "mutual club" or carrying on a trading activity or an adventure in the nature of trade" is largely a question of fact [Wilcock's case - 9 Tax Cases 111, (132) C.A. (1925) (1) KB 30 at 44 and 45]." (Emphasis supplied)

33. In our opinion, unlike the aforesaid surplus amount itself, which is exempt from tax under the doctrine of mutuality, the amount of interest earned by the assessee from the afore-noted four banks will not fall within the ambit of the mutuality principle and will therefore, be exigible to Income-Tax in the hands of the assessee-club.

34. In light of the afore-going discussion, these appeals are bereft of any merit and are thus, liable to be dismissed. Accordingly, we dismiss all the appeals with costs.

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|                    |       (D.K. JAIN, J.)                  |
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|                    |       (JAGDISH SINGH KHEHAR, J.)       |
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|NEW DELHI,          |                                        |
|JANUARY  14, 2013.  |                                        |
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[1] AIR 1948 PC 142 (E)
[2] (2000) 3 SCC 214
[3] [1889] 2 TC 460

[4] [1926] 12 T.C. 841 (H.L.)
[5] (1918) 24 CLR 334
[6] AIR 1954 SC 85
[7] (1932) 16 TC 430, 448 (HL); CIT v. Firozepur Ice Manufacturers' Association 84 ITR 607

[8] 1927 AC 827

[9] (1934) 18 TC 499; 503, 506
[10] (1997) 5 SCC 394
[11] (1927) 11 TC 790
[12] AIR 1965 SC 96