

**Commissioner of Income-tax, Madras-ii Vs. Madras Co-operative House Construction Society Ltd.**

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**Court :** Chennai

**Decided On :** Aug-11-1976

**Reported in :** [1978]111ITR187(Mad)

**Appeal No. :** Tax Case No. 368 of 1970 (Reference No. 118 of 1970)

**Appellant :** Commissioner of Income-tax, Madras-ii

**Respondent :** Madras Co-operative House Construction Society Ltd.

**Judgement :**

ISMAIL J. - The Income-tax Appellate Tribunal, Madras Bench, under section 66(1) of the Indian Income-tax Act, 1922, has referred the following question of law for the opinion of this court :

'Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the whole income from house properties and interest of the society consisted of profits of the business carried on by it and that it should be exempted within the terms of the notification dated August 25, 1925, issued under section 60 of the Indian Income-tax Act, 1922 ?'

The facts which gave rise to the above question are as follows : The assessee in this case is a co-operative society registered under the provisions of the Madras Co-operative Societies Act, 1932. The activities of the society as found by the Tribunal which has referred to the bye-laws of the society, are as follows :

'The society was formed to acquire lands and to set up a housing colony. For this purpose it raised resources not only from its members, but also largely by way of loans from Government. The assessee acquired a large piece of land and laid it out in plots. The society undertook to build three kinds of houses for the benefit of its members and it is important to note that the members themselves did not build the houses. The society carried out repairs to the house, whether they were annual or of a special kind. We have already held that the society was the owner of these properties till the member who had entered into a hire purchase agreement paid various instalments to the society which covered its expenses on account of interest or otherwise.

The society provided certain common services and amenities to the members including a primary school. The bye-laws show that the society was entitled to make profits by selling a portion of the land for the purpose of markets, shops, etc., and utilise the profits for certain common purposes. Like every co-operative society whose affairs are watched by the Registrar the assessee kept a nominal margin of only one

per cent. between the interest paid by it to the Government on the loans and received by it from the members and it may be that this feature as well as the rest of the conduct of the affairs of the society were designed to keep the profits at the minimum and at the same time ensure that losses were not incurred; all the same it is clear that the society entered into extensive operations over a period of years involving lakhs of rupees and the conduct of complex transactions with members and outsiders. In its accounts for the relevant years, the assessee has displayed on the assets side of the balance-sheet, land of the value of more than Rs. 36 lakhs, completed buildings of the value of more than Rs. 89 lakhs and work-in-progress for building of the value of more than Rs. 25 lakhs. It also displayed on the assets side of the balance-sheet the stock of building materials and heavy equipment acquired for the purpose of the construction. The value of the amenities account as shown in the balance-sheet is more than Rs. 12 lakhs. Considering the entire conduct of the affairs of the society, we are of the opinion that the buildings were held by the society in the course of its business which consisted of acquiring land, erecting buildings, hiring them out and selling them. In the course of this business the assessee was obliged to raise loans on interest and recouped itself by charging interest on the instalments due from its members to whom some of the buildings were allotted. All these transactions are in our view a part and parcel of the same activity. Thus, the whole of the income of the society consists of profits of the business carried on by it and whatever may be the head of income under which a portion thereof may fall to be considered, it has to be exempted within the terms of the notification dated August 25, 1925. In this view of the matter we have to accept the contention of Shri Swaminathan in support of the order of the Appellate Assistant Commissioner.'

In this case, what happened was that the Income-tax Officer treated the houses built by the society as belonging to the society and the income which it received as income falling under section 9 of the Indian Income-tax Act, 1922, and assessed the same to tax. Only in respect of the interest income which it received, the Income-tax Officer treated it as the income from business and exempt under the notification referred to above, whose terms we shall set out later. On appeal preferred to the Appellate Assistant Commissioner, the Appellate Assistant Commissioner took the view that the houses belonged to the allottees and, therefore, the income referable to the houses cannot be assessed in the hands of the society. With the result, he set aside the assessment made by the Income-tax Officer. As against the order of the Appellate Assistant Commissioner, the department preferred an appeal to the Tribunal. The Tribunal, after considering the terms of the hire purchase agreements entered into between the allottees of houses and the society, came to the conclusion that till the last instalment of the hire purchase amount was paid by the allottee and a conveyance executed by the society in favour of the allottee, it is the society which continued to be the owner of the houses built by it. Notwithstanding this conclusion, the Tribunal held that the income which the society received was exempt as per the notification referred to above.

Section 60 of the Indian Income-tax Act, 1922, so far as it is relevant states that the Central Government may, by notification in the official Gazette, make an exemption, reduction in rate of other modification, in respect of income-tax in favour of any class of income, or in regard to the whole or any part of the income of any class of persons. In exercise of the powers conferred by this section the Central Government issued the notification dated 25th August, 1925, and the said notification is as follows :

'The following classes of income shall be exempt from the tax payable under the said

Act (Indian Income-tax Act, 1922) but shall be taken into account in determining the total income of an assessee for the purposes of the said Act :- .....

(2) The profits of any co-operative society other than the Sanikatta Salt Owners' Society in the Bombay Presidency for the time being registered under the Co-operative Societies Act, 1912 (II of 1912), the Bombay Co-operative Societies Act, 1925 (Bombay Act VII of 1925), or the Madras Co-operative Societies Act, 1932 (Madras Act VI of 1932), or the dividends or other payments received by the members of any such society out of such profits.

Explanation. - For this purpose the profits of a co-operative society shall not be deemed to include any income, profits or gains from -

(1) investments in, (a) securities of the nature referred to in section 8 of the Indian Income-tax Act; or (b) property of the nature referred to in section 9 of that Act,

(2) dividends, or

(3) the other sources referred to in section 12 of the Indian Income-tax Act.'

The question for consideration is whether the income received by the society is exempt from income-tax under the provisions of this notification or not. It can be seen that the notification generally exempts the profits of any co-operative society other than the Sanikatta Salt Owners' Society in the Bombay Presidency for the time being registered under the Co-operative Societies Acts referred to above, though the said income has to be taken into account in determining the total income of the assessee for the purposes of the Income-tax Act. From the scope of this exemption, what are excepted are the enumerated categories of income mentioned in the Explanation. It is not in dispute that the only relevant excepted category falling within the scope of the Explanation will be item 1 (b), namely, investments in property of the nature referred to in section 9 of the Indian Income-tax Act, 1922. Consequently, if it is established that the income received by the co-operative society in the present case is income from investments in the houses which it had built, only then the co-operative society will be liable to tax in respect of the income in question and otherwise, irrespective of the particular head under which the income may fall, it will be exempted. From the bye-laws of the society it is clear that the building of the houses by the society was not by way of investment. The very object of the society was to relieve the housing shortage and for that purpose it formed itself into a co-operative society registered under the Madras Co-operative Societies Act and, with the assistance of loans advanced by the Government on concessional rates of interest, it purchased lands and built houses and allotted the houses to its members on hire-purchase basis. Such a transaction cannot be said to be an investment by the co-operative society in building houses. Therefore, on the basis that the houses belonged to the co-operative society till the last instalment of the hire purchase amount was paid by the allottee and a conveyance was executed by the society in favour of the allottee, the income from the houses cannot be said to be income investment by the society in property of the nature referred to in section 9 of the Indian Income-tax Act, 1922. Once the income in the present case does not fall under that head it is not disputed that the income will be exempt from tax under the terms of the notification referred to already. We may incidently point out that in view of the opening portion of the notification not referring to the profits and gains of a business, it is not even necessary to decide whether the income actually received by the co-operative society in the present case

is income from business or not. All that is necessary for the purpose of deciding the eligibility for exemption in the present case under the terms of the notification is whether the income derived by the co-operative society can be said to be income from investments in property of the nature referred to in section 9 of the Indian Income-tax Act, 1922. As we have already held that the income of the society is not income from investments in property of the nature referred to in section 9 of the Indian Income-tax Act, 1922, the assessee was rightly held to be entitled to the exemption provided for in the notification.

Under these circumstances, the question referred to this court is answered in the affirmative and in favour of the assessee. The assessee will be entitled to the costs of this reference. Counsel's fee is fixed at Rs. 500.

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