

Story of Young Indian – Cancellation of Section 12AA Registration

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The Honourable Delhi ITAT¹ in the matter of Young Indian v CIT (Exemption)² has confirmed the rejection of registration under Section 12AA of Income Tax Act, 1961 (Act) with retrospective effect is valid in law. In this article, we discuss the story of Young Indian (YI), the acquisition of Associated Journals Limited (AJL), the non-carrying of any activities of YI and the cancellation of registration of YI with retrospective effect.

YI was incorporated as a company under Section 25 of Companies Act, 1956. Memorandum of Association was subscribed by two directors, namely Mr Suman Dubey and Mr Satyam Gangaram Pitroda with 550 equity shares each. Post incorporation, both the shareholders transferred their shares to Mr Oscar Fernandes and Mrs Sonia Gandhi (SG). Subsequent to such transfer, Mr Suman Dubey and Mr Satyam Gangaram Pitroda were appointed as directors of a company, M/s Associated Journals Limited (AJL). Later, Mr Rahul Gandhi (RG) was appointed as director of YI and also acquired 3600 shares of YI. Simultaneously, SG has further acquired shares totalling to 3600 shares of YI and also become a director of YI.

As on 31.03.2010, AJL owes an amount of Rs 88.86 Crores to All India Congress Committee (AICC). AJL has further taken a loan from AICC totalling the outstanding to Rs 90 Crores. The share capital of AJL was Rs 1 Crore. AICC has transferred the outstanding loan of Rs 90 Crores from AJL for a consideration of Rs 50 lakhs to YI. Later, the share capital of AJL was increased to Rs 10 Crores and the additional shares were allotted to YI (99.99%) giving the maximum control of AJL to YI. The balance shares were subscribed by SG, RG and Mrs Priyanka Gandhi (PG).

The dates of the events detailed in this article is tabulated as under for easy comprehension:

Date	Event	Remarks
14.10.2010	Application for Incorporation of YI	Initial subscribers (IS) as Mr Dubey and Mr Pitroda
23.11.2010	Incorporation of YI	-
-	Transfer of Shares by IS	Transfer to Mr Oscar Fernandes & Mrs Sonia Gandhi
13.12.2010	Appointment of RG as director of YI	RG acquired 3600 shares of YI and also became director
16.12.2010	Transfer of OL to YI	AICC transferred OL due from AJL to YI for Rs 50 lakhs
21.12.2010	Appointment of IS as directors of AJL	Mr Dubey and Mr Pitroda appointed as directors of AJL
31.03.2010	Outstanding Loans (OL) in AJL	Rs 88.86 Crores from AICC as outstanding loans
22.01.2011	Appointment of SG as director of YI	SG further acquired shares and became director of YI
01.03.2011	Availment of Loan by YI – Rs 1 Crore	Loan from M/s Dotex Merchandise Private Limited
01.03.2011	Payment of Rs 50 lakhs to AICC	YI has paid said amount for purchase of OL due from AJL
31.03.2011	Application of YI under 12AA	For registration as charitable institution
06.05.2011	Grant of registration - Section 12A	YI has obtained registration with effective from AY 11-12
21.03.2016	Suo moto surrender of 12AA by YI	In absence of foreseeable surpluses, YI surrendered

¹ Income Tax Appellate Tribunal

² ITA No 7751/Del/2017

YI having the main objective to inculcate in the minds of Indian Youths commitment to the ideal of a democratic and secular society in conformity with the ideals of Mahatma Gandhiji and Pt. Jawahar Lal Nehru, has applied for registration under Section 12AA before DIT (E)³. A show cause notice was served asking YI to furnish certain information along with the note on activities to be performed. YI has replied to the said notice and stated that the proposed activities are charitable in nature as defined under Section 2(15) and accordingly prayed for grant of registration. The address mentioned in the application filed by YI is the same address where AJL is located and the Chairman of AJL has given no-objection certificate to YI to carry on their activities from their premises. The Learned DIT (E) has granted the registration certificate under Section 12A read with Section 12AA subjected to certain conditions, where one of such condition is that the registration shall be liable to be cancelled if it is found that the said registration is obtained fraudulently by misrepresentation or suppression of facts.

YI in its 5th year has written to DIT (E) stating that they hold shares of AJL and such investment was never intended for gain and since there were no available significant surpluses in foreseeable future, they intend to suo moto surrender the registration under Section 12A read with Section 12AA.

In 2017, the CIT (E)⁴ has issued show cause notice to YI asking them to explain whether there were any change in the aim and objectives of YI during AY 11-12 to 16-17 and since the only activity done by YI was to acquire 99.99% shares of AJL, which is engaged in real estate business and whether earning of income from real estate business is within the main objectives and aims of YI and whether such activities are in conformity with the terms and conditions subject to which registration under Section 12A is granted to YI.

YI has replied to the said notice stating that just because investment was made in AJL, it cannot be said that YI is engaged in business of real estate and the surrendering of the registration does not mean that YI is not engaged in commercial activities and the reason for surrender is that they do not foresee any significant surplus and nothing else.

CIT (E) on a perusal of the reply filed by the YI and examining the annual accounts filed for the period 11-12 to 14-15 has observed that YI has not incurred any expenditure for meeting their objectives except for creating provision for interest payments for the loan taken by YI to purchase the shares of AJL. CIT (E) for the period ended 31.03.2011 has observed that YI has incurred an amount of Rs 50 lakhs for the pursuit of its objectives. The notes to account states that YI has acquired loan owed of Rs 90 Crores by AJL from AICC for a consideration of Rs 50 lakhs and as a part of restructuring exercise of AJL, the said loan was converted into ordinary shares and allotted to YI. The notes further states that since said acquisition is treated as application on the objects of YI, the same has not been reflected as an investment in shares. Further, CIT (E) has examined the activities carried out by AJL and noted that said company was engaged in publishing newspapers and ceased such activity with effective from 02.04.2008. After such cessation of publication, the income of AJL was engaged in purchase, construction, sale and renting out of properties and has prominent properties in major cities in India.

Accordingly, CIT (E) has stated that the since the substantial shares of AJL was held by YI, it can be stated that YI is engaged in business of real estate business through its subsidiary. The acquisition of shares of AJL cannot be said to be in pursuit of the objectives of YI, the said expenditure cannot be treated as applied for the purposes for which YI was incorporated. He further held that the voluntary registration was a consequence of mounting pressure from the tax department qua investigation and re-opening of assessment of YI. Accordingly, the CIT (E) held that activities of YI were not genuine and

³ Director of Income Tax (Exemption)

⁴ Commissioner of Income Tax (Exemption)

not carried out in accordance with the objects and cancelled the registration with effective from AY 11-12 denying the expenditure incurred amounting to Rs 50 lakhs and also claim of exemption of Rs 2 Crores which is collected as annual fee.

YI and tax authorities have made extensive arguments before the Honourable ITAT and framed the question for discussion as to whether CIT (E) is justified in law and facts in cancelling the registration granted under Section 12 and Section 12AA with effective from AY 11-12, which amounts to retroactive cancellation. The only challenge from YI is that the act of cancellation of registration under Section 12A read with Section 12AA with effective from AY 11-12 is bad and accordingly prayed before the Honourable ITAT to set aside the order of CIT (E).

The Honourable ITAT after pursuing the order, other documents and hearings from both the sides, stated that the YI at the time of application of registration under Section 12A read with Section 12AA has not brought out the fact that the YI has purchased outstanding loan of AJL due to AICC for a nominal consideration of Rs 50 lakhs, that YI has taken a loan of Rs 1 Crore and no assets or liabilities were shown in the balance sheet of YI and the allotment of shares by AJL to YI. Since all the material facts were concealed the DIT (E) has granted the registration. If at all YI has brought all the material facts without suppressing them, the DIT (E) may have not granted the registration in first place. Since the registration granted is subjected to certain conditions, where one of such condition is that the registration would be subjected for cancellation, if it is later discovered that the registration is obtained basis of suppression of material facts.

The Honourable ITAT further stated that YI never in its replies filed before the CIT (E) has substantiated that the objectives of AJL were in alignment with the objectives of YI and has never claimed that it does not have any ownership interest, whatsoever, in the properties owned by AJL, which makes it abundantly clear that the YI had other intentions. The ITAT has also brushed away YI's contention that acquisition of AJL was to spread democratic and secular values to youths of India through the medium of newspapers published by AJL, since the majority of the publication of AJL has started after the surrender of registration of YI. Hence, the ITAT has held that was an afterthought and did not give weightage to the additional evidences filed by YI.

The Honourable ITAT further held that the CIT (E) has rightly observed that YI has failed to show at least one activity which was done during the period 11-12 to 15-16 in pursuit of its objectives except purchasing AJL. Hence, it is inferable that entire move is for acquiring AJL, which has stopped publishing activities and was holding large number of properties worth hundred of crores with huge rental income was for acquiring control and interest in such properties for mere sum of Rs 50 lakhs and asked whether prudence justify such acquisition was for furtherance of charity or for furtherance of the objects of YI? The ITAT has further stated that if the intention of YI in acquiring AJL was in pursuit of YI's objectives, then what was the reason to hide such transaction and purchase of AJL loan for Rs 50 lakhs also does not look like a genuine transaction.

The Honourable ITAT then proceeded to examine the judgments put forth by the tax authorities. One of them was the judgment of Honourable Single Judge of Delhi High Court which has upheld the eviction notice issued by Land Development Officer on AJL on the premise that there was no printing activity which is being continued by AJL in such property. AJL has preferred appeal against the judgment of Honourable Single Judge and the Honourable Delhi High Court speaking through its Chief Justice has upheld the judgment of Honourable Single Judge and made an important observation holding that there is no hesitation in holding that the purpose for which the doctrine of lifting the veil is applied is nothing but a principle followed to ensure that a corporate character or personality is misused as a device to conduct something which is improper and not permissible in law, fraudulent in

nature and goes against public interest and is employed to evade obligations imposed in law. Seen in above context, the High Court held that the take over of loan due to AICC for Rs 50 lakhs and thereafter replacing the original shareholders of YI by four new entities including Sh. Moti Lal Vohra, Chairman of AJL and YI after acquiring 99% shares in AJL, became the main shareholder with four of its shareholders acquiring the administrative right to administer property of more than Rs 400 Crores and thereby held that entire transaction of transferring shares of AJL to YI was nothing but, a clandestine and surreptitious transfer of lucrative interest in the premises to YI.

Basis the judgement of Honourable Delhi High Court, the ITAT has held that conduct of YI from the incorporation till the application for registration under Section 12AA, was not to carry out any charitable activity, but to acquire huge assets of hundreds of crores for a negligible amount. Seeking a status of charitable institution and obtaining registration under Section 12AA, with such kind of conduct clearly indicates that it is a misuse of law and some kind of colourable device. The ITAT further held that there is another angle which requires consideration, is that why YI was pressing for registration under Section 12AA only for the said five years and why they have voluntarily surrendered the registration in 2016.

The ITAT further held that the plea of YI that CIT (E) does not have power to cancel the registration with retrospective effect does not hold good, because the provisions of Section 12AA (3), wherein it provides that the Commissioner has statutory powers to cancel the registration under Section 12A/12AA, if he finds reasons to believe that the activities are not in line with the objects or activities carried out are not genuine in nature. The ITAT has placed reliance on the judgment of Honourable High Court in the matter of Prathyusha Educational Trust vs Principal Commissioner of Income Tax, Central -2, Chennai⁵, wherein it was held as under:

19. The next contention of Mr. Anirudh Krishnan is that the cancellation of the exemption under Section 10(23C)(vi) of the Act and cancellation of the registration under Section 12AA of the Act with retrospective effect is illegal.

*At the first blush, the Court assumed that the argument of Mr. Anirudh Krishnan is to the effect that the cancellation/withdrawal was with effect from the date of grant of exemption/registration. **However, on a perusal of the order dated 18.11.2014 withdrawing the approval granted under Section 10(23C)(vi) of the Act, it is seen that it has been given effect to from the assessment year 2010-2011. Likewise the order cancelling the assessee's registration under Section 12AA of the Act is from the assessment year 2010-2011. Can it be said that these orders of cancellation are with retrospective effect. The definite answer for this question is an emphatic 'No'. Admittedly, the business premises of the assessee was subjected to search during the assessment year 2010-2011. The Assessing Officer while completing the assessment found large scale diversion of funds and several improper actions on the part of the assessee in direct conflict to the terms of the Deed of Trust and conditions of registration/exemption. Therefore, it was recommended to the competent authority to initiate proceedings for cancellation of the exemption/registration. The matter was decided after due opportunity to the assessee and speaking orders have been passed and obviously these orders will take effect from the assessment year 2010-2011 and it is a mis-nomer to state that the orders are retrospective or retroactive. The lis which was the subject matter is for the assessment year 2010-2011 and though the orders of cancellation of the exemption/registration was passed on 18.11.2014 and 07.12.2016 they would take effect from the assessment year 2010-2011 during which year the cause of action arose...***

⁵ 2019 (7) TMI 302- Madras High Court

(emphasis supplied by us)

Since YI has not done any activity in pursuit of its objects, the ITAT has held that Commissioner is empowered to cancel the registration from such date and accordingly held that the act of Learned CIT (E) in cancelling the registration with effect from past date is in accordance with the law.