CHARITABLE OR RELIGIOUS TRUSTS AND INSTITUTIONS, POLITICAL PARTIES AND ELECTORAL TRUSTS

LEARNING OUTCOMES

After studying this chapter, you would be able to -

- **appreciate** the conditions to be fulfilled by universities, other educational institutions, hospitals and other medical institutions to claim the benefit of exemption under section 10(23C);
- **identify** the inclusions in the definition of “charitable purpose”, to appreciate whether a trust or institution would qualify for the benefit of exemption under sections 11 and 12;
- **appreciate** the conditions to be fulfilled by a trust or institution to claim benefit of exemption under section 11;
- **appreciate** the procedure to be followed for registration of a trust or institution;
- **examine** the special provisions relating to taxability of anonymous donations received by a trust or institution;
- **appreciate** the special provisions for taxability of accreted income of certain trusts and institutions;
- **analyse and apply** the above provisions to compute the total income and tax liability of trusts and institutions and address related issues;
- **identify** the income of political parties which are exempt from tax and the conditions to be satisfied to avail the exemption;
- **examine** the conditions to be satisfied by an electoral trust to avail exemption in respect of voluntary contributions received by it;
- **apply** the above provisions relating to political parties and electoral trusts in making computations and addressing related issues.
13.1 INTRODUCTION
Section 10(23C), *inter alia*, exempts income received by any person on behalf of university, or other educational institution or any hospital. Section 11 provides exemption in respect of income derived from property held under trust wholly for charitable or religious purposes. Section 13A exempts certain categories of income derived by a political party and section 13B exempts voluntary contributions received by electoral trusts.

13.2 INCOME OF UNIVERSITIES, HOSPITALS, EDUCATIONAL INSTITUTIONS, MEDICAL INSTITUTIONS ETC. [SECTION 10(23C)]
As we have read in Chapter 3, exemption is available in respect of any income received by any person on behalf of the certain funds and institutions. In particular, in this chapter, we would be dealing with income of universities, educational institutions, hospitals and other medical institutions covered under sub-clauses (iiiab), (iiiac), (iiiad), (iiiae), (iv), (v), (vi) and (vii) of section 10(23C):

1. any university or other educational institution wholly or substantially financed by the Government which exists solely for educational purposes and not for profit [Sub-clause (iiiab)];

2. any hospital or other institution wholly or substantially financed by the Government, which exists solely for philanthropic purposes and not for profit and which exists for the reception and treatment of persons suffering from illness or mental defectiveness or for the reception and treatment of convalescing persons or persons requiring medical attention or rehabilitation [Sub-clause (iiiac)];

If the government grant to a university or other educational institution, hospital or other institution during the relevant previous year exceeds 50% of the total receipts (including any voluntary contributions), of such university or other educational institution, hospital or other institution, as the case may be, then, such university or other educational institution, hospital or other institution shall be considered as being *substantially financed by the Government* for that previous year.

3. any university or other educational institution existing solely for educational purposes and not for profit and its aggregate annual receipts do not exceed ₹ 1 crore [Sub-clause (iiiad)];

4. any hospital or other institution as described in (2) above if its aggregate annual receipts do not exceed the prescribed limit of ₹ 1 crore [Sub-clause (iiiae)];

5. any other fund or institution for charitable purposes approved by the prescribed authority having regard to the objects of the fund or institution and its importance throughout India or throughout any State or States [Sub-clause (iv)];
any trust (including any other legal obligation) or institution wholly for public religious or wholly for public religious and charitable purposes approved by the prescribed authority having regard to ensure the income applies for the objects of the fund or institution [Sub-clause (v)];

any other university or educational institution existing solely for educational purposes and not for purposes of profit and which may be approved by the prescribed authority [Sub-clause (vi)];

any other hospital, or other medical institution as described in (2) above approved by the prescribed authority [Sub-clause (via)].

Notes:

(i) Application in prescribed form: The application form for such exemption will have to be made in the prescribed form and manner.

(ii) Commissioner of Income-tax (Exemptions) to act as “prescribed authority” for the purpose of section 10(23C)(iv)/(v)/(vi)/(via): Commissioner of Income-tax (Exemptions) is empowered to call for such documents or information as it considers necessary in order to satisfy itself about the genuineness of the activities of the fund or trust or institution or any university or other educational institution or any hospital or other medical institution, and the compliance of such requirements under any other law for the time being in force by such fund or trust or institution or any university or other educational institution or any hospital or other medical institution, as the case may be, as are material for the purpose of achieving its objects before approving the same under section 10(23C)(iv)/(v)/(vi)/(via). Such documents may include audited annual accounts. The prescribed authority may also make such inquiries as it may deem necessary for this purpose.

(iii) Conditions to be fulfilled for exemption: For exemption under section 10(23C)(iv)/(v)/(vi)/(via), the fund or trust or institution etc. must fulfill the following conditions:

(a) It should apply its income or accumulate it for application wholly and exclusively to the objects for which it is established,

(b) In case where more than 15% of its income is accumulated, the period of accumulation of the amount exceeding 15% of its income shall be maximum 5 years.

(c) Funds should be invested or deposited in the forms or modes specified in section 11(5). This condition would however not apply to the following funds—

any assets held by the fund, trust or institution or any university or other educational institution or any hospital or other medical institution, where such assets form part of the corpus of the fund, trust or institution or any university or other educational institution or any hospital or other medical institution as on 1.6.1973;
— any asset, being equity shares of a public company, held by any university or other educational institution or any hospital or other medical institution where such assets form part of its corpus as on 1.6.1998;
— any debentures, issued by or on behalf of any company or corporation, acquired by the fund, trust or institution, etc. before 1.3.1983;
— any bonus shares allotted to the fund, trust or institution, etc. in respect of the shares mentioned above forming part of the corpus of such fund, etc.
— voluntary contributions received and maintained in the form of jewellery, furniture or other article as the Board may specify for any period during the previous year.

(iv) **Applicability of exemption to profits and gains of business of the trust/fund etc.** - Exemption under section 10(23C)(iv)/(v)/(vi)/(via) would not apply to profits and gains of business in all cases. However, where the business is incidental to the attainment of its objectives and separate books of account are maintained in respect of the business, the exemption would apply to such business profits also.

(v) **Period of validity of notification issued by the Central Government** - Any notification issued by the Central Government [under sub-clauses (iv) or (v)] on or after 13.7.2006 will be valid until withdrawn.

(vi) **Time limit for passing order of approval/rejection** - Where an application form for exemption is made on or after 13.7.2006, every notification under sub-clause (iv)/(v) shall be issued or approval under sub-clause (iv)/(v)/(vi)/(via) shall be granted or an order rejecting the application shall be passed within the period of 12 months from the end of the month in which such application was received.

(vii) **Audit of accounts** - If the total income of any entity referred to in sub-clauses (iv), (v), (vi) and (via) of section 10(23C), without giving effect to the provisions of the said sub-clauses, exceeds the basic exemption limit in any previous year, it shall –

1. get its accounts audited in respect of that year by a chartered accountant; and
2. furnish such audit report along with the return of income for the relevant assessment year. The report must be in the prescribed form, duly signed and verified by the accountant, and must contain such particulars as may be prescribed.

(viii) **Payment or credit to another fund, trust etc. out of accumulated income not to be considered as application of income** - Where the fund/ trust/ institution/ university/ hospital etc. does not apply its income during the year of receipt and accumulates it, and subsequently makes a payment or credit out of such accumulated income, to any institution or trust registered u/s 12AA or to any fund/ trust/ institution/ university/ hospital, such payment or credit shall not be considered to be an application of income for its specified objectives.
(ix) **Provisions of sections 40(a)(ia), 40A(3) and 40A(3A) apply in case of application of income by Fund/ Trust/ Institution etc.** – In case where an expenditure is incurred on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or after deduction, has not been paid on or before the due date under section 139(1), 30% of sum paid would not be treated as application of income in that year. The same would be, however, be treated as application in the year in which tax is deducted and paid.

Likewise, where the trust/fund etc. incurs any expenditure in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque/bank draft/ECS, exceeds ₹ 10,000, the same would not be considered as application of income.

Further, where any liability incurred has been allowed as application during the P.Y., say P.Y. 2019-20 and subsequently, say during the P.Y. 2020-21, the trust/fund/institution etc. makes payment in respect thereof, otherwise than by way of account payee cheque/bank draft/ECS, payment so made shall be deemed as income of the trust/fund/institution etc. of the year in which payment is made, if the payment or aggregate of payments made to a person in a day exceeds ₹ 10,000.

(x) **Withdrawal of approval** - The Central Government, or prescribed authority shall have the power to withdraw the approval or rescind the notification if:

(a) such fund/ institution/university/hospital etc. has not applied its income or invested/ deposited its funds in accordance with the provisions; or

(b) the activities of such fund, etc. are not genuine; or

(c) such activities are not being carried out in accordance with the conditions based upon which it was notified or approved; or

(d) **such fund/institution/university/hospital etc. has not complied with the requirement of any other law for the time being in force, and the order, direction or decree, by whatever name called, holding that such non-compliance has occurred, has either not been disputed or has attained finality**

However, the approval or notification can be withdrawn or rescinded only after issuing a show cause notice and giving reasonable opportunity to such fund, etc. of being heard. After withdrawing the approval or rescinding the notification, a copy of the order is to be forwarded to the concerned fund/institution, etc. as well as to the Assessing Officer.

(xi) **Time limit for making an application for grant of exemption** - The time limit for making an application for grant of exemption or continuation thereof under section 10(23C) by a fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clauses (iv)/(v)/(vi)/(via) of section 10(23C) has been specified in respect of such applications made on or after 1.6.2006. Such applications have to be filed on or before 30th September of the succeeding financial year. For example,
if an educational institution seeks exemption under clause (vi) for P.Y.2019-20 (i.e. A.Y.2020-21), it has to make an application for grant of exemption by 30.9.2020.

(xii) **Anonymous donation to be included in total income** - Any anonymous donation referred to in section 115BBC on which tax is payable in accordance with the provisions of the said section shall be included in the total income.

(xiii) **Amount credited or paid out of income of any fund, trust etc. by way of corpus donation to any trust or institution registered under section 12AA not considered as application** - Any amount credited or paid out of income of any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv)/(v)/(vi)/(via), to any trust or institution registered under section 12AA, being voluntary contribution made with a specific direction that they shall form part of the corpus of the trust or institution, shall not be treated as application of income to the objects for which such fund or trust or institution or university or educational institution or hospital or other medical institution, as the case may be, is established.

(xiv) **Trust not entitled to exemption if its commercial receipts exceed 20% of total receipts** - If the purpose of a trust or institution referred to in sub-clauses (iv)/(v) of section 10(23C) does not remain charitable in a previous year on account of the commercial receipts exceeding 20% of total receipts of the trust or institution, then, such trust or institution would not be entitled to get benefit of exemption in respect of its income for that previous year in which the commercial receipts exceed the specified threshold. The denial of exemption would be compulsory by operation of law and would not be dependent on any approval being withdrawn or registration being cancelled or a notification being rescinded.

Such trust and institution cannot get benefit of tax exemption in the year in which its receipts from commercial activities exceed 20% of total receipts, whether or not the registration or approval granted or notification issued is cancelled, withdrawn or rescinded in respect of such trust or institution.

(xv) **No benefit of exemption under section 10 to entities eligible for exemption under section 10(23C)** - Entities which have been approved or notified for claiming benefit of exemption under section 10(23C) would not be entitled to claim any benefit of exemption under any other provision of section 10 [except exemption under section 10(1) in respect of agricultural income]. This is to ensure that once a trust or institution voluntarily opts for the special dispensation under this section, it should be governed by these provisions and should not be allowed the flexibility of being governed by the general provisions of section 10. Allowing such flexibility may have adverse effects on the objective for which this section was enacted.

(xvi) **Depreciation not allowable if cost of asset claimed as application** - Income for the purposes of application under section 10(23C) shall be determined without allowing any deduction or allowance for depreciation or otherwise, where the cost of acquisition of the
asset has been claimed as application of income under section 10(23C) in the same previous year or any other previous year.

**ILLUSTRATION 1**

An educational institution having annual receipts of ₹ 1.20 crore during the P.Y. 2019-20, has to make an application to the prescribed authority before 31.3.2020 for claiming tax exemption under section 10(23C). Discuss the correctness or otherwise of this statement.

**SOLUTION**

This statement is **not** correct.

According to the first proviso to section 10(23C), an educational institution having aggregate annual receipts exceeding ₹ 1 crore, is required to make an application to the prescribed authority for grant of exemption under section 10(23C)(vi). Further, it is provided that such application can be made on or before 30th September of the relevant assessment year from which the exemption is sought.

Therefore, in the given case, the educational institution (having annual receipts of ₹ 1.20 crore during the P.Y. 2019-20) can make an application for grant of exemption in the prescribed form to the prescribed authority on or before 30th September, 2020, for claiming exemption under section 10(23C)(vi) for previous year 2019-20.

**13.3 CHARITABLE OR RELIGIOUS TRUSTS AND INSTITUTIONS [SECTIONS 11 TO 13]**

(1) **General discussion on trusts** - Before considering the provisions of sections 11 to 13 which govern the exemption in respect of income from property held for charitable or religious purposes, let us see briefly what exactly the term trust signifies, the types of trusts and the manner of their creation. Though this aspect of the topic does not strictly fall within the purview of income-tax, such a general knowledge would be useful in understanding the provisions of tax laws relating to charitable trusts.

A trust is an obligation annexed to the ownership and arising out of a confidence reposed in and accepted by the owner if declared and accepted by him for the benefit of another or of another and the owner. The person who reposes or declares the confidence is called the ‘author of the trust’; the person who accepts the confidence is called the trustee; the person for whose benefit the confidence is accepted is called the ‘beneficiary’; the subject matter of the trust is called the ‘trust property’; the ‘beneficial interest’ or ‘interest’ of the beneficiary is his right against the trustees or owner of the trust property and the instrument, if any, by which trust is declared is called the ‘instrument of trust’.

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Trusts can be broadly classified into two groups - Public and Private. The distinction between a public and private trust is that, whereas in the former, the beneficiaries are the general public or a class thereof, in the latter they are specific individuals. While in the former the beneficiaries constitute a body which is incapable of ascertainment, in the latter they are persons who are ascertained or capable of being ascertained. In some cases, private trusts may enure for the benefit of the public. Some religious trust may also be in the nature of public-cum-private trust.

Private trusts are governed by the Indian Trust Act, 1882. This Act does not apply to the following:

1. The rules of Mohammedan law as to waqf;
2. The mutual relations of the members of undivided family as determined by any customary or personal law;
3. Public or private religious or charitable endowments; and
4. Trust to distribute prizes taken in war among the captors.

From the above, it will be clear that public charitable trusts are not governed by the Indian Trust Act.

There are three requirements for creation of a public trust. They are (1) a declaration of trust which is binding on the settlor, (2) setting apart definite property and depriving himself of the ownership, and (3) a statement of objects for which the property is thereafter to be held. In the case of a private trust also, more or less similar requirements exist.

The word ‘trust’ as used in the context of sections 11 to 13 includes, in addition to the ‘trust’ as explained above, ‘any other legal obligation’. This is made clear in Explanation 1 to section 13. The words ‘any other legal obligation’ are wide enough to cover Muslim wakfs, Hindu endowments and dedications to deities. It would also cover a case in which the trustees of a settlement are to pay the income to other trustees who in their turn are bound to apply it for purposes which are religious or charitable.

(2) **Tax Exemption [Section 11]** - Subject to the provisions of sections 60 to 63, the income of a religious or charitable trust or institution, to the extent specified in the Act, is exempt from tax when certain prescribed conditions are fulfilled. The relevant income does not even form part of the total income of the trust or institution.

Section 11 deals with the exemption of income from property held in trust or other legal obligation for religious or charitable purposes wholly or in part. Section 12 deals with exemption of income derived by such a trust from voluntary contributions. Section 12A prescribes the conditions as to registration of trust etc. Section 13 enumerates the circumstances under which the exemption available under sections 11 to 12 will be denied.

(i) **Income from property held for charitable or religious purposes** - The following income shall not be included in the total income of the previous year of the person in receipt of the income:
(a) Income derived from property held under trust wholly for charitable and religious purposes to the extent such income is applied in India for such purpose.

(b) Income derived from property held under trust in part only for such purpose, to the extent such income is applied in India for such purposes. However, the trust in question must have been created before 1.4.1962.

(c) Income derived from property held under trust, created on after 1.4.1952 for charitable purpose which tends to promote international welfare in which India is interested to the extent to which such income is applied to such purpose outside India. This does not cover religious trusts.

Income derived from property held under a trust for charitable or religious purposes, created before 1.4.1952, to the extent to which such income is applied for such purposes outside India.

In both the cases, the CBDT should have, by general or special order, directed that such income shall not be included in the total income of the person in receipt of such income.

(d) Income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution.

Thus, it may be noted that only such income derived from property held under trust wholly for charitable or religious purposes is exempt. If the property is held in part only for such purposes, it is necessary that such a trust must have been created before the commencement of the Act. In both the cases, the exemption is limited to the extent such income is applied in India for such specified purposes.

(ii) Types of trusts - To get exemption in respect of income applied outside India, the trusts are divided into two types:

(a) If the object of the trust is to promote international welfare in which India is interested, such trust may have been created on or after 1.4.1952.

(b) If the trust is for any other charitable purpose it must have been created before 1.4.1952. Here also, the exemption is limited to the extent to which such income is applied outside India for such specified purposes. It is to be noted however that a direction from CBDT by a general or special order is necessary before such exemption can be claimed.

(iii) Conditions for claiming exemption

(a) Property should be held under trust - The exemptions explained in the preceding paragraphs are available if and only if there is a valid trust or there is a legal obligation, under which the income derived from the property held under such trust or legal obligation is to be applied for charitable or religious purposes. If there is no
trust nor any legal obligation, the income will not be exempt even if the whole of such
income is applied to charitable or religious purposes. A mere creation of a trust for
the income is not sufficient, there must be a trust of the property out of which the
income is derived before one can consider any exemption under section 11.

(b) **Income should be applied for charitable purposes** - Section 2(15) states that
‘charitable purpose’ includes relief of the poor, education, yoga, medical relief,
preservation of environment (including watersheds, forests and wildlife) and
preservation of monuments or places or objects of artistic or historic interest and the
advancement of any other object of general public utility.

The definition of “charitable purpose” includes “any other object of general public
utility” The question arises as to what is an object of “general public utility”. This
expression has not been defined anywhere in the Act.

In *CIT v. Gujarat Maritime Board* (2007) 295 ITR 561, the Supreme Court observed
that the Gujarat Maritime Board was established for the predominant purpose of
development of minor ports within the State of Gujarat, the management and control
of the Board was essentially with the State Government and there was no profit
motive. The assessee, Gujarat Maritime Board, was under a legal obligation to apply
its income which was directly and substantially from the business held under trust for
the development of minor ports in Gujarat. Therefore, the Supreme Court held that
the assessee was entitled to be registered as “charitable trust” under section 12A.

A number of entities functioning on commercial basis claim exemption of their income
either under section 10(23C) or section 11 on the foundation that they are charitable
institutions. This is based on the contention that they are engaged in the “advancement
of an object of general public utility” as is included in the fourth part of the present
definition of “charitable purpose”. There were many decisions rendered in the past
supporting the view that if unconnected business is held under a trust for promoting the
object of general public utility and if profits are used for promoting such objects,
income thereof shall be exempt, for example, the decision of the Supreme Court in *CIT
v. Madras Stock Exchange Ltd.* (1981) 130 ITR 184. However, such a claim in respect
of an activity carried out on commercial basis, goes against the basic intention of the
provision.

Therefore, in order to limit the ambit of the phrase “advancement of any other object of
general public utility”, section 2(15) provides that “the advancement of any other object
of general public utility” would not be a charitable purpose if it involves the carrying on of

- (a) any activity in the nature of trade, commerce or business or,
- (b) any activity of rendering of any service in relation to any trade, commerce or
business,
for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity, or the retention of such income, by the concerned entity.

Thus, the advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income from such activity, unless,-

(1) such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility; and

(2) the aggregate receipts from such activity or activities, during the previous year, does not exceed 20% of the total receipts of the trust or institution undertaking such activity or activities, for the previous year.

Therefore, in effect, “advancement of any other object of general public utility” would continue to be a “charitable purpose“, if the activity in the nature of trade, commerce or business is undertaken in the course of actual carrying out of such advancement of any other object of general public utility and the aggregate receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed 20% of the total receipts of the trust or institution undertaking such activity or activities, for the previous year.

**ILLUSTRATION 2**

An institution having its main object as “advancement of general public utility” received ₹ 30 lakhs in aggregate during the P.Y.2019-20 from an activity in the nature of trade. The total receipts of the institution, including donations, was ₹ 140 lakhs. It applied 85% of its total receipts from such activity during the same year for its main object i.e. advancement of general public utility.

(i) What would be the tax consequence of such receipt and application thereof by the institution?

(ii) Would your answer be different if the institution’s total receipts had been ₹ 150 lakhs (instead of ₹ 140 lakhs) in aggregate during the P.Y.2019-20?

(iii) What would be your answer if the main object of the institution is “relief of the poor” and the institution receives ₹ 30 lakhs from a trading activity, when its total receipts are ₹ 140 lakhs and applies 85% of the said receipts for its main object?
SOLUTION

(i) As the main object of the institution is “advancement of object of general public utility”, the institution will lose its “charitable” status for the P.Y.2019-20, since it has received ₹ 30 lakhs from an activity in the nature of trade, which exceeds ₹ 28 lakhs, being 20% of the total receipts of the institution undertaking that activity for the previous year. The application of 85% of such receipt for its main object during the year would not help in retaining its “charitable” status for that year. The institution will lose its charitable status and consequently, the benefit of exemption of income for the P.Y.2019-20, irrespective of the fact that its approval is not withdrawn or its registration is not cancelled.

(ii) If the total receipts of the institution is ₹ 150 lakhs, and the institution receives ₹ 30 lakhs in aggregate from an activity in the nature of trade during the P.Y.2019-20, then it will not lose its “charitable” status since receipt of upto 20% of the total receipts of the institution in a year from such activity is permissible. The institution can claim exemption subject to fulfilment of other conditions under sections 11 to 13. Further, such activity should also be undertaken in the course of actual carrying out of such advancement of any other object of general public utility.

(iii) The restriction regarding carrying on of a trading activity for a cess, fee or other consideration will not apply if the main object of the institution is “relief of the poor”. Therefore, receipt of ₹ 30 lakhs from a trading activity by such an institution will not affect its “charitable” status, even if it exceeds 20% of the total receipts of the institution. The institution can claim exemption subject to fulfilment of other conditions under sections 11 to 13.

ILLUSTRATION 3

(a) “Save Wild Life” an institution having its main object as ‘preservation of wildlife’, used the entire income derived from an activity in the nature of trade for its main object during the previous year ended on 31.03.2020. Would such utilization of its income be treated as utilisation for “charitable purpose”? Examine. Would your answer be different, if the main object of the institution is “advancement of object of general public utility”?

(b) A charitable trust derives its income from the business of providing mineral water to various companies situated in Software Technology Park in Hyderabad. A sum of ₹ 30 lacs has been derived as net income from such business activity, which has been applied for the object of general public utility. The total receipts of the trust during the P.Y. 2019-20 was ₹ 140 lakhs. Examine the taxability of application of the income, if the income so derived relates to the previous year 2019-20. Would your answer be different, if the trust runs a school in a backward district and applies the profits from the business for such school’s activity?
(a) Section 2(15) defines “charitable purpose” to include relief of the poor, education, yoga, medical relief, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest and the advancement of any other object of general public utility. However, the “advancement of any other object of general public utility” shall not be a charitable purpose, if the institution is carrying on any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income derived from such activity.

Therefore, preservation of wildlife is included in the definition of “charitable purpose” under section 2(15). Further, an institution having the preservation of wildlife as its main object would not be subject to the restrictions which are applicable to the “advancement of any other object of general public utility”. Such institution would continue to retain its “charitable” status, even if it derives income from an activity in the nature of trade.

However, if an institution having its main object as “advancement of any other object of general public utility”, derives income from an activity in the nature of trade during a financial year, it would lose its “charitable” status for that year, even if it applies such income for its main objects.

It may be noted that if the receipts from such activity does not exceed 20% of the total receipts in that year, then, the institution would not lose its “charitable” status, even if its main object is “advancement of any other object of general public utility”, if such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility.

(b) In the first case, net income from the business of supplying mineral water to various companies i.e., ₹30 lakhs is not eligible for exemption under section 11, since the receipt from such activity exceeds 20% of total receipts (i.e., 20% of ₹140 lakhs) during the year. This is because “advancement of any object of general public utility” would not be a charitable purpose if it involves carrying on of any activity in the nature of trade, commerce or business, for example, supply of mineral water for a consideration, as in this case. It is immaterial that the net income from such business is applied for the object of general public utility.

On the other hand, where the trust runs a school in a backward district, this restriction is not applicable. The reason is that the restriction contained in section 2(15) is applicable only to the last limb of the definition of “charitable purpose” i.e. advancement of object of general public utility. It does not affect the other limbs of the definition viz. “relief of the poor”, “education”, “medical relief” etc.
Section 11(4) clarifies that “property held under trust” includes a business undertaking so held. As per section 11(4A), exemption can be availed in respect of profits and gains of business, if such business is incidental to the attainment of the objectives of the trust and separate books of account are maintained in respect of such business. Therefore, in the second case, the profit from the business shall be eligible for exemption under section 11, assuming that the said business is incidental to the attainment of the objects of the trust (i.e., education) and books of account for such business activity is maintained separately.


Exemption under section 11 in case of an assessee claiming both to be a charitable institution as well as a mutual organisation

The proviso to section 2(15) will apply only to entities whose purpose is advancement of any other object of general public utility i.e. the last limb of the definition of charitable purpose contained in section 2(15). Hence, such entities will not be eligible for exemption under section 11 or under section 10(23C), if they carry on commercial activities. Whether such an entity is carrying on an activity in the nature of trade, commerce or business is a question of fact which will be decided based on the nature, scope, extent and frequency of the activity.

There are industry and trade associations who claim exemption from tax under section 11 on the ground that their objects are for charitable purpose as these are covered under any other object of general public utility. Under the principle of mutuality, if trading takes place between persons who are associated 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, then any surplus returned to the persons forming such association is not chargeable to tax. In such cases, there must be complete identity between the contributors and the participants.

Therefore, where industry or trade associations claim to be both charitable institutions as well as mutual organizations and their activities are restricted to contributions from and participation of only their members, these would not fall within the purview of the proviso to section 2(15) owing to the principle of mutuality. However, if such organizations have dealings with non-members, their claim to be charitable organizations would be governed by the additional conditions stipulated in the proviso to section 2(15).

In the final analysis, however, whether the assessee has, for its object, the advancement of any other object of general public utility is a question of fact. If such assessee is engaged in any activity in the nature of trade, commerce or business or renders any service in relation to trade, commerce or business, it would not be entitled to claim that its object is charitable purpose. In such a case, the object of general public utility will be only a mask or a device
to hide the true purpose which is trade, commerce or business or the rendering of any service in relation to trade, commerce or business. Each case would, therefore, be decided on its own facts and no generalization is possible.

Circular No.395, dated 24.9.1984 – Promotion of sports and games is considered to be a charitable purpose within the meaning of section 2(15). Therefore, an association or institution engaged in the promotion of games and sports can claim exemption under section 11 even if it is not approved under section 10(23).

A trust will be treated as a charitable trust under section 2(15) even if its object involves the carrying on of an activity for profit. Such a trust will not be denied exemption under section 11 on the ground that its objects are non-charitable.

(iv) **Application and accumulation** - We have seen that the exemption is limited to the extent to which such income is applied in India or outside India, as the case may be. Is it necessary that the entire income should be so applied? The Act gives a concession here. It is possible to claim the exemption even if the trust or institution applies only 85% of the income derived from the trust property for the purpose of the trust, during the relevant previous year.

An accumulation not exceeding 15% of the income from such property is permissible. For computing this 15%, voluntary contributions referred to in section 12 shall be deemed to be part of the income. It must be clearly noted that accumulation must be with the object of application of the accumulated amount for charitable or religious purpose in India at a later date. Such a facility for accumulation is not available for those trusts whose income is to be applied outside India.

(v) **Inability to apply in full 85% of the income** - It is clear from the above discussion that free accumulation not exceeding 15% of income from property is permissible. Hence, the balance 85% must be applied during the previous year for the purposes for which the trust has been created. However, it is possible that the trust is unable to apply the minimum of 85% of its income during the previous year due to either of the following reasons.

1. The whole or any part of the income has not been received during that year.
2. Any other reason.

In the first class of cases, the period of application is extended to cover the previous year in which the income is actually received and the previous year immediately following the year. However, the amount which may be so claimed to have been so applied during the subsequent previous year cannot exceed the amount of the income which had not been

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1 As per the Supreme Court ruling in *CIT v. Programme for Community Organisation (2001) 116 Taxman 608*, 15% of gross receipts would be eligible for accumulation under section 11(1)(a).
received earlier but received during a subsequent previous year. In the second case, the period of application is extended to the previous year immediately following the previous year in which the income was derived.

Example

During the previous year ending 31st March, 2020, a charitable trust earned an income of ₹1,00,000 but it received only ₹60,000 in that year. The balance of ₹40,000 is received in the year ending 31-3-2021.

Solution

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total income earned during the P.Y.2019-20</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Actual receipt in P.Y.2019-20</td>
<td>60,000</td>
</tr>
<tr>
<td>Permissible accumulation @15% of ₹1,00,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Balance to be applied during P.Y.2019-20</td>
<td>45,000</td>
</tr>
</tbody>
</table>

Amount received in P.Y.2020-21 to be applied in P.Y.2020-21 or P.Y.2021-22 40,000

Since this amount of ₹40,000 is received during the P.Y. 2020-21, this can be applied in the P.Y.2020-21 or in the P.Y.2021-22. If the entire amount of ₹40,000 is duly spent for charitable purposes in these two years, the exemption is fully available but if only part of the amount is so spent within the period, the exemption is restricted to that part only.

There may be a case where the inability springs from some other reason e.g., late receipt of the income making it impossible to spend it before the end of the year.

Example

A trust receives a sum of ₹50,000 on 30th March, 2020. Its previous year ends on 31-3-2020.

Solution

It is obvious that it is impossible to apply the requisite sum within one day. Therefore, it has been provided that such sum can be applied at any time during the immediately following previous year i.e., up to 31-3-2021.

(vi) Amount credited or paid out of income of any trust by way of corpus donation to any trust or institution registered under section 12AA not considered as application - Any amount credited or paid, out of income derived from property held under trust, to any trust or institution registered under section 12AA, being voluntary contribution made with a specific direction that they shall form part of the corpus of the trust or institution, shall not be treated as application of income for charitable or religious purpose.

(vii) Provisions of sections 40(a)(ia), 40A(3) and 40A(3A) apply in case of application of income by trust – In case where an expenditure is incurred on which tax is deductible at
source under Chapter XVII-B and such tax has not been deducted or after deduction, has not been paid on or before the due date under section 139(1), 30% of sum paid would not be treated as application of income in that year. The same would be, however, be treated as application in the year in which tax is deducted and paid.

Likewise, where the trust incurs any expenditure in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque/ bank draft/ ECS, exceeds ₹ 10,000, the same would not be considered as application of income.

Further, where any liability incurred has been allowed as application during the P.Y., say P.Y. 2019-20 and subsequently, say during the P.Y. 2020-21, the trust makes payment in respect thereof, otherwise than by account payee cheque/bank draft/ECS, payment so made shall be deemed as income of the trust of the year in which payment is made, if the payment or aggregate of payments made to a person in a day exceeds ₹ 10,000.

(viii) **Procedural Formalities: Exercise of option** - To avail the facility of the extended period of application of income, the trust has to exercise an option in writing that the income applied later as prescribed may be deemed to be income applied to the relevant charitable purposes during the previous year in which the income was derived. Such option has to be exercised before the expiry of the time allowed statutorily under section 139(1).

The income so deemed to have been applied shall, however, not be taken into account in calculating the amount of income applied to such purposes, during the previous year in which the income is actually received or during the immediately following previous year, as the case may be. Thus, in the Example 1 given above, the amount of ₹ 40,000, received subsequently in the year 2020-21 and applied to charitable purposes in the year 2020-21, will by virtue of the option exercised by the trust, be deemed to be applied for charitable purposes in the year 2019-20 itself. Therefore, such an amount will not be taken into consideration in determining the amount of income applied for charitable purposes in the year 2020-21.

Section 11(1B) provides that where the income for which an option has been exercised as discussed above, is not actually applied, it is to be treated as the income of the previous year immediately following the year of receipt or the previous year in which it was derived, as the case may be.

(ix) **Conditional accumulation** - As per section 11, application of income derived from property held under trust for charitable purposes in India is the main condition for grant of exemption to trust or institution in respect of income derived from property held under such trust. In case such income cannot be applied during the previous year, the same can be accumulated and applied for such purposes, subject to satisfaction of the conditions provided therein.
Section 11 permits accumulation of 15% of the income indefinitely by the trust or institution. However, 85% of income can only be accumulated for a period not exceeding 5 years subject to the conditions that such person submits the prescribed form i.e., Form 10 to the Assessing Officer and the money so accumulated or set apart is invested or deposited in the specified forms or modes.

If the accumulated income is not applied for charitable purposes or ceases to be accumulated or set apart for accumulation or ceases to remain invested or deposited in specified modes, then, such income is deemed to be taxable income of the trust or institution.

For the purpose of clarifying the period within which the assessee is required to file Form 10, and to ensure due compliance of the above conditions within time, section 11(2) provides that -

(1) such person should furnish a statement in the prescribed form and in the prescribed manner to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is being accumulated or set apart, which shall, in no case, exceed five years.

In computing the period of five years, the period during which the income could not be applied for the purpose for which it is so accumulated or set apart, due to an order or injunction of any court, shall be excluded.

(2) the money so accumulated or set apart should be invested or deposited in the modes specified in section 11(5).

(3) the statement in Form 10 should be filed on or before the due date of filing return of income specified under section 139(1).

In case the statement in Form 10 is not submitted on or before this date, then, the benefit of accumulation would not be available and such income would be taxable at the applicable rate. Further, the benefit of accumulation would also not be available if return of income is not furnished on or before the due date of filing return of income specified in section 139(1) [Section 13(9)].

**ILLUSTRATION 4**

A charitable institution registered under section 12AA of the Income-tax Act, 1961 filled in Form No.10 for seeking permission to accumulate unapplied income under section 11(2) of the Act for the objects of the institution and submitted it to the Assessing Officer along with the resolution for accumulation. The Assessing Officer found that the objects for which accumulation was sought were not particularised in as much as they covered the entire range of objects of the institution. Can the Assessing Officer deny the benefit of accumulation in such a case?
SOLUTION

Section 11(2) permits a charitable trust or institution to accumulate its unspent income where 85% of the income is not applied or is not deemed to have been applied to charitable or religious purposes in India during the previous year. The institution or trust has to specify, by notice in writing given to the Assessing Officer, the purpose for which the income is being accumulated or set apart and the period for which such income is to be accumulated or set apart.

In the given case, the assessee institution sought the permission of the Assessing Officer to accumulate unapplied income for the objects of the institution. The institution had not stated any objects in particular for which the unspent income was sought to be accumulated or set apart. In *Bharat Krishak Samaj vs. Deputy Director of Income-tax (Exemption)* (2008) 306 ITR 153 (Del.), it was held that it is not necessary for a charitable trust to particularize each and every object for which accumulation is sought. It is enough if the assessee seeks permission for accumulation for the objects of the trust. Therefore, the Assessing Officer cannot deny the benefit of accumulation in such a case.

**Modes specified in section 11(5):**

1. Investment in Government Saving Certificates.
2. Deposits with Post Office Savings Banks.
3. Deposit with Scheduled banks or Co-operative Banks.
4. Investment in units of the Unit Trust of India.
5. Investment in Central or State Government Securities.
6. Investments in debentures issued by or on behalf of any company or corporation. However, both the principal and interest thereon must have been guaranteed by the Central or the State Government.
7. Investment or deposits in any public sector company.

Where an investment is made in the shares of any public sector company and such public sector company ceases to be a public sector company, the investment so made shall be deemed to be an investment made for a period of three years from the date of such cessation and in the case of any other investment or deposit, till the date of its maturity.

8. Investment in bonds of approved financial corporation providing long term finance for industrial development in India and eligible for deduction under section 36(1)(viii).
9. Investment in bonds of approved public companies whose principal object is to provide long-term finance for construction or purchase of houses in India for residential purposes and eligible for deduction under section 36(1)(viii).
(10) Deposits with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for urban infrastructure in India.

"Long-term finance" means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years.

"Urban infrastructure" means a project for providing potable water supply, sanitation and sewerage, drainage, solid waste management, road, bridges and flyovers or urban transport.

(11) Investment in immovable property excluding plant and machinery, not being plant and machinery installed in a building for the convenient occupation thereof.

(12) Deposits with Industrial Development Bank of India.

(13) Any other mode of investment or deposit as may be prescribed. Rule 17C specifies the following other modes: (1) Investments in units issued under any scheme of mutual fund referred to in section 10(23D); (2) Any transfer of deposits to Public Account of India; (3) Deposits made with an authority constituted in India or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or for both; (4) investment by way of acquiring equity shares of a ‘depository’; (5) investment by a recognized Stock Exchange, in the equity shares of a company promoted by it to acquire the membership rights of other stock exchanges, where at least 51% of the paid-up share capital is held by the Stock Exchange and the balance is held by its members; (6) investment by way of acquiring equity shares of an incubatee by an incubator; (7) investment by way of acquiring shares of National Skill Development Corporation; (8) investment in debt instruments issued by any infrastructure finance company registered with RBI; (9) investment in Stock Certificate as defined in of Sovereign Gold Bonds Scheme, 2015.

**Amount credited or paid, out of accumulated income of any trust, to any trust or institution registered under section 12AA or referred to in section 10(23C)(iv)/(v)/(vi)/(via), not considered as application of income [Explanation to section 11(2)]**

Any amount credited or paid, out of income derived from property held under trust, which is not applied, but is accumulated or set apart, to any trust or institution registered under section 12AA or to any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv)/(v)/(vi)/(via) of section 10(23C), shall not be treated as application of income for charitable or religious purpose, either during the period of accumulation or thereafter.
Deemed income in case of non-utilisation or mis-utilisation of accumulated amount

Where the accumulated income of the trust -

(a) is applied for purposes other than charitable or religious purposes; or

(b) ceases to be accumulated or set apart for application thereto; or

(c) ceases to remain invested or deposited in any of the modes mentioned under section 11(5) above; or

(d) is not utilised for the purpose for which it is so accumulated or set apart during the period specified (not exceeding 5 years) or in the year immediately following thereof.

However, in computing the aforesaid period of 5 years, the period during which the income could not be applied for the purposes for which it is so accumulated or set apart due to an order or injunction of any Court shall be excluded.

(e) accumulated or set apart for application to charitable and religious purposes in India, is credited or paid to any trust or institution registered under section 12AA or to any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv)/(v)/(vi)/(via) of section 10(23C),

such income shall be deemed to be the income of the previous year –

(a) in which it is so applied; or

(b) in which it ceases to be accumulated or set apart; or

(c) in which it ceases to remain so invested or deposited; or

(d) immediately following the expiry of the period aforesaid; or

(e) in which it is paid or credited.

In DIT (Exemption) v. Khetri Trust (2014) 367 ITR 723 (Del), properties bequeathed to a trust could not be transferred to it due to ongoing court litigation and pendency of probate proceedings question arose if violation of the provisions of section 11(5) be attracted. In the facts of the case, trustees paid ₹ 1,10,000 for raising a memorial for late Raja Bahadur Sardar Singh and the said amount was given to a business entity for this purpose, but due to the ongoing dispute, such project was not completed the Commissioner (Appeals) observed that the validity of the will has been challenged in the probate proceedings; therefore, till the ‘will’ is probated and affirmed as genuine, the trust would not acquire the legal right on the property for the purpose of Act. In case the probate is denied, the properties would not devolve on the trust. The shares in foreign company were still in the name of the donor, late assessee and its acquisition by the trust is dependent upon the adjudication of the probate.
Further, with regard to the advance given to the business entity, the Commissioner (Appeals) found that the said amount cannot be treated as an investment which was covered and regulated by section 11(5), since the intent and purpose behind the payment was not investment. Based on the above factual findings, elucidated and affirmed by the Commissioner (Appeals) and the Tribunal, the High Court held that there was no violation of section 11(5) in this case.

**Application to be made to Assessing Officer for application of income for other purposes**

It is possible that due to circumstances beyond the control of the person in receipt of the income, any income invested or deposited in approved modes cannot be applied for the purpose for which it was accumulated or set apart. In such a case, an application may be made to the Assessing Officer specifying such other purposes as are in conformity with the objects of the trust. The Assessing Officer may allow the application of income to such other purposes. If such a permission is granted by the Assessing Officer, the new purposes will be deemed to be purposes specified in the written notice given to the Assessing Officer.

It is to be noted that the Assessing Officer cannot allow transfer of any such accumulated income to other charitable trusts/institutions as application of income towards charitable purposes. This has created genuine problems for those trusts and institutions which are wound up. However, in case of a trust or institution which has invested or deposited its income in any of the forms mentioned in section 11(5), the Assessing Officer can allow application of such income for crediting or payment to any trust or institution registered under section 12AA or any fund or institution or trust or university or education institution or hospital or medical institution covered by section 10(23C). Such application can be allowed only in the year in which such trust or institution is dissolved.

(x) **No deduction for depreciation where cost of asset has been claimed as application of income** - Income for the purposes of application under section 11 shall be determined without allowing any deduction or allowance for depreciation or otherwise, in respect of any asset, the cost of acquisition of which has been claimed as an application of income under this section in the same or any other previous year [Section 11(6)].

**ILLUSTRATION 5**

MSO Foundation, a charitable institution set up on 1st April, 2019 and registered under section 12AA with effect from that date, is engaged in providing education in hotel management. The organisation acquires a building for using the same for holding classes and office activities. It has approached you for your opinion on its eligibility to claim the cost of the building and also depreciation thereon in the current year and the subsequent year. Advise the institution indicating the reasons.
SOLUTION

(i) 15% of income from property held for charitable purposes is exempt from tax under section 11. The remaining 85% of such “income” would be exempt if it is “applied” for charitable purposes in India.

(ii) Application of the amount can be for revenue or capital purposes. As long as the expenditure is incurred out of income earned by the trust and for the purposes of carrying on the objects of the trust, it would be treated as application of income even if such expenditure is for capital purposes. Therefore, since the building is acquired by the organization for holding classes and office activities, which is for the purposes of carrying on the objects of the charitable institution i.e., for providing education in hotel management, the cost of the building would be treated as application of income.

However, section 11 provides that where the cost of building is claimed as application, no other deduction for depreciation or otherwise would be allowed as an application of income in respect of such asset for the same or any other previous year.

(xii) **Charitable trust engaged in business activity [Section 11(4A)]** - Consequently, a charitable trust engaged in business activity will be liable to any tax on income from the activity. However, exemption would be available to the trust in respect of income earned from such business activity if –

(a) such business is incidental to the attainment of the objects of the trust/institution; and

(b) Where the income determined by the Assessing Officer is in excess of that shown in the books of the undertaking, such excess shall be deemed to be applied to purposes other than charitable or religious purposes.
(b) separate books of account are maintained by such trust/institution in respect of such business.

*Note* – Profits derived by a trust/institution referred to in clauses (21), (23A), (23B), (23BB) and (23C) of section 10 will continue to be exempt from income-tax, since section 11(4A) does not override the provisions of section 10.

(xiv) **Instances where capital gains would be deemed to have been applied for charitable purposes [Section 11(1A)]**

(a) **Transfer of a capital asset held under trust wholly for charitable or religious purposes [Section 11(1A)(a)]** - Where the whole of the net consideration from the transfer of the capital asset is utilised for acquiring a new capital asset which is held under trust wholly for charitable or religious purposes, the entire amount of capital gains arising from the transfer would be deemed to have been applied for charitable or religious purposes. If, however, only a part of the net consideration is utilised in acquiring the new capital asset, the amount of capital gains deemed to have been utilised for charitable or religious purposes shall be equal to the excess of the proceeds utilised over the cost of the asset transferred.

<table>
<thead>
<tr>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Original cost of capital asset transferred</strong></td>
</tr>
<tr>
<td><strong>Consideration for which it is transferred</strong></td>
</tr>
<tr>
<td><strong>Situation 1 Cost of new capital asset acquired</strong></td>
</tr>
<tr>
<td><strong>Situation 2 Cost of new capital asset acquired</strong></td>
</tr>
</tbody>
</table>

**Amount that will be deemed to have been applied for charitable purposes.**

- **Situation 1** ₹ 50,000
- **Situation 2** ₹ 20,000

(b) **Transfer of a capital asset held under trust in part only for charitable and religious purposes [Section 11(1A)(b)]** - Where only a part of a capital asset has been transferred, only the “appropriate fraction” of the capital gain arising from the transfer shall be deemed to have been applied to charitable or religious purposes. Where the whole of the net consideration is utilised in acquiring the new capital asset, the whole of the appropriate fraction of such capital gain will be deemed to have been so applied. In any other case, the exemption will be limited to so much of the appropriate fraction of the amount utilised for acquiring the new asset as exceeds the appropriate fraction of the cost of the transferred asset.

“Appropriate fraction” means the fraction which represents the extent to which the income derived from the capital asset transferred was applicable to charitable or religious purposes before such transfer.
**Example**

A capital asset is being held under trust. Two-thirds of the income derived from such capital asset are being utilised for the charitable purposes of the trust. The asset is being transferred.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of transferred asset</td>
<td>₹ 1,20,000</td>
</tr>
<tr>
<td>Net consideration</td>
<td>₹ 1,80,000</td>
</tr>
<tr>
<td>Cost of new asset acquired</td>
<td>₹ 1,50,000</td>
</tr>
<tr>
<td>Capital gains</td>
<td>₹ 60,000</td>
</tr>
<tr>
<td>Appropriate fraction</td>
<td>2/3rd</td>
</tr>
</tbody>
</table>

Income represented by ‘appropriate fraction’ = 2/3rds of ₹ 60,000 = ₹ 40,000

Since the entire net consideration has not been utilised in acquiring the new asset, the amount deemed to have been utilised for charitable purpose will be (2/3rds of ₹ 1,50,000) – (2/3rds of ₹ 1,20,000) = ₹ 1,00,000 – ₹ 80,000 = ₹ 20,000.

(xv) **Voluntary Contributions [Section 12]** - Any voluntary contribution received by a trust created wholly for charitable or religious purposes or by an institution established wholly for such purposes shall, for the purposes of section 11, be deemed to be income derived from property held under trust wholly for charitable or religious purposes. However, corpus donations (i.e. contributions made with a specific direction that they shall from part of the corpus of the trust or institution) shall not be treated as income. Such corpus donations are treated as capital receipts not chargeable to tax. Other voluntary contributions would be treated as income. However, exemption can be claimed in respect of such income subject to fulfillment of the conditions mentioned below –

(a) The trust should be registered under section 12AA with the Principal Commissioner or Commissioner of Income-tax;

(b) If the total income of the trust exceeds the basic exemption limit, the accounts of the trust should be audited.

(c) The trust should apply at least 85% of its income for the approved purposes.

(d) The balance should be invested or deposited in specified forms or modes.

**Note** – It may be noted that the corpus donations are to be considered for the purpose of determining whether the accounts of the trust are to be audited. Further, corpus donations have to be invested only in the investments approved under section 11(5). If invested elsewhere, the income from unapproved investment would be chargeable to tax.
ILLUSTRATION 6

Hundi (charitable box) superscribing “contributions in this hundi form part of corpus of trust fund” kept at Lord Venkateshwara Temple, Tirumala, was opened on 30.3.2020. Cash of ₹ 100 lakhs and valuable articles worth ₹ 250 lakhs were found to have been contributed by the devotees. Discuss the tax implications.

SOLUTION

As per section 11(1)(d), income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution shall not be included in the total income of the recipient. In the given case, there is a specific declaration by the temple authorities that the contributions being put in the hundi (charity box) would form part of the corpus of the trust fund. Therefore, it is possible to take a view that those who put the contributions in the hundi give a tacit declaration that the contributions would form part of the corpus. Hence, a view can be taken that such contributions shall not be included in the total income of the recipient trust.

Further, it may be noted that the provision relating to taxability of anonymous donations under section 115BBC does not apply to voluntary contributions received by a trust or institution created or established wholly for religious purposes.

(3) Conditions for applicability of sections 11 & 12 [Section 12A]

(i) Conditions to be satisfied and the assessment year from which exemption would be available: The exemption provisions contained in section 11 and 12 as explained above shall not apply in relation to the income of any trust or institution unless the following conditions are satisfied:

(a) In respect an application for registration of trust was made before 1.6.2007, the requirement was that such application had to be made one year from the date of creation of the trust and the exemption provisions of section 11 and 12 applied from the date of creation of the trust or establishment of the institution [Section 12A(1)].

(b) This requirement of filing an application for registration under section 12A within one year of creation of the religious or charitable trust or institution has been removed in respect of applications made on or after 1.6.2007. The application can be filed at any time now.

(c) Accordingly, in respect of applications filed in the prescribed form to the Principal Commissioner or Commissioner on or after 1st June, 2007, the provisions of sections 11 and 12 would apply from the assessment year relevant to the financial year in which the application is made i.e., the exemption would be available only with effect from the assessment year relevant to the previous year in which the application is filed. It would not be available in respect of any earlier assessment year [Section 12A(2)].
Thus, under section 12A, a trust or an institution can claim exemption under sections 11 and 12 only after registration under section 12AA has been granted. Also, in case of trusts or institutions which apply for registration after 1st June, 2007, the registration shall be effective only prospectively.

(ii) **Fresh registration of a trust in the event of adoption or undertaking modifications of the objects after the registration has been granted [Section 12A(ab)]**: Where a trust or an institution has been granted registration under section 12AA or has obtained registration at any time under section 12A [as it stood before its amendment by the Finance (No. 2) Act, 1996] and, subsequently, it has adopted or undertaken modifications of the objects which do not conform to the conditions of registration, it shall be required to obtain fresh registration by making an application within a period of thirty days from the date of such adoption or modification of the objects, to the Principal Commissioner or Commissioner, in the prescribed form and manner.

(iii) **Circumstance when exemption would be granted for an earlier assessment year**

Non-application of registration for the period prior to the year of registration causes genuine hardship to charitable organisations. On account of non-registration, tax liability gets attracted in those years even though they may otherwise be eligible for exemption due to compliance with other substantive conditions. Further, condonation of delay in seeking registration is also not permitted. Therefore, three provisos have been inserted in section 12A by the Finance (No.2) Act, 2014, in order to remove the genuine hardship and provide relief to the trusts.

In case where a trust or institution has been granted registration under section 12AA, the benefit of sections 11 and 12 shall be available in respect of any income derived from property held under trust in any assessment proceeding for an earlier assessment year which is pending before the Assessing Officer as on the date of such registration.

(a) **Condition for grant of such exemption:**

The objects and activities of such trust or institution in the relevant earlier assessment year should be the same as those on the basis of which such registration has been granted.

(b) **Reassessment proceedings not to be initiated for earlier years due to reason of non-registration**

No action for reopening of an assessment under section 147 shall be taken by the Assessing Officer in the case of such trust or institution for any assessment year preceding the first assessment year for which the registration applies, merely for the reason that such trust or institution has not obtained the registration under section 12AA for the said assessment year.
Non-availability of above benefits to a trust or institution in certain cases

The above benefits would, however, not be available in case of any trust or institution which at any time had applied for registration and the same was denied or a registration granted to it was cancelled at any time under section 12AA.

ILLUSTRATION 7

Can a trust created for charitable purposes in April 2019, having filed application for registration as per section 12A on 11.4.2020, claim benefits of sections 11 and 12 from Assessment Year 2020-21?

SOLUTION

In respect of applications filed on or after 1st June, 2007, the provisions of sections 11 and 12 shall apply from the assessment year relevant to the financial year in which the application is made i.e., the exemption would be available only with effect from the assessment year relevant to the previous year in which the application is filed. It would not be available in respect of any earlier assessment year.

Therefore, since the trust has filed application for registration only on 11.4.2020, it cannot claim benefit of sections 11 and 12 from A.Y.2020-21. Assuming that the registration has been granted under section 12AA, the exemption would be available only from the A.Y. 2021-22, being the assessment year relevant to the previous year in which application is filed [i.e., P.Y. 2020-21].

However, where a trust has been granted registration under section 12AA in the P.Y. 2020-21, the benefit of sections 11 and 12 shall be available in respect of any income derived from property held under trust for assessment year 2020-21, being the assessment year preceding the assessment year in which application is filed i.e., A.Y.2021-22, if assessment proceedings in respect of that year is pending before the Assessing Officer as on the date of such registration.

It may be noted that exemption in respect of an earlier assessment year can be claimed only if the objects and activities of such trust or institution in the relevant earlier assessment year are the same as those on the basis of which such registration has been granted.

ILLUSTRATION 8

Help All, a trust created on 1st January, 2020 for providing relief to the poor, applied for registration under section 12A on 1st March, 2020. On that date, its corpus fund comprised only of the initial contribution made by the trustees. The Commissioner denied registration solely on the ground that the trust had not commenced any charitable activity, due to which he could not satisfy himself about the genuineness of the trust. Is the ground for denial of registration by the Commissioner justified in this case? Discuss.
SOLUTION

The Karnataka High Court, in *DIT (Exemptions) v. Meenakshi Amma Endowment Trust (2013) 354 ITR 219*, opined that an application under section 12A for registration of the trust can be sought even within a week of its formation. The activities carried on by the trust are to be seen in a case where the registration is sought much later after formation of the trust.

The High Court further observed that the corpus fund included contribution made by the trustees only, which indicated that the trustees were contributing the funds by themselves in a humble way and were intending to commence charitable activities. The assessee-trust had not also collected any donation for the activities of the trust, by the time its application came up for consideration before them. When the application for registration was made, the trust, therefore, did not have sufficient funds for commencement of its activities.

The High Court observed that, with the money available with the trust, it cannot be expected to carry out activity of charity immediately. Consequently, in such a case, it cannot be concluded that the trust has not intended to do any activity of charity. In such a situation, where application is made shortly after formation of the trust, the objects of the trust as mentioned in the trust deed have to be taken into consideration by the authorities for satisfying themselves about the genuineness of the trust and not the activities carried on by it. Later on, if it is found from the subsequent returns filed by the trust, that it is not carrying on any charitable activity, it would be open to the concerned authorities to withdraw the registration granted or cancel the registration as per the provisions of section 12AA(3).

Applying the rationale of the above ruling, the Commissioner cannot deny registration solely on the ground that the trust had not commenced any charitable activity in this case, since the trust has applied for registration under section 12A within two months after its formation and the corpus fund comprised only of contribution made by the trustees. The Commissioner has to take into consideration the objects of the trust as mentioned in the trust deed to satisfy itself about the genuineness of the trust.

(iv) **Audit** - Where the total income of the trust without giving effect to the provisions of section 11 and 12 exceeds the maximum amount which is not chargeable to income-tax in any previous year, the accounts of the trust must be audited by a chartered accountant and the report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such prescribed particulars, should be furnished along with the return.

(v) **Mandatory filing of return**: In order to provide further clarity, section 12A provides for further condition that the person in receipt of the income chargeable to income-tax shall furnish the return of income within the time allowed under section 139(4A) of the Act.

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(4) **Procedure for Registration [Section 12AA]** - The Principal Commissioner or Commissioner, on receipt of an application for registration of a trust or institution made under section 12A(1) shall proceed as follows:

(i) He would call for such documents or information from the trust or institution as he thinks necessary in order to satisfy himself about—

(a) the genuineness of activities of the trust or institution and

(b) the compliance of such requirements of any other law for the time being in force by the trust or institution as are material for the purpose of achieving its objects

and may also make such enquiries as he may deem necessary in this behalf.

(ii) After satisfying himself about the objects of the trust or institution and the genuineness of its activities as required in (i)(a) above and compliance of the requirements under (i)(b) above, he shall pass an order in writing registering the trust or institution.

(iii) If he is not satisfied, he shall pass an order in writing refusing to register the trust or institution.

(iv) A copy of such an order issued under (ii) or (iii) above shall be sent to the applicant. However, an order under (iii) shall not be passed unless the applicant has been given a reasonable opportunity of being heard.

(v) Every order granting or refusing registration shall be passed within six months from the end of the month in which the application for registration of trust or institution is received by the Principal Commissioner or Commissioner.

(vi) Where a trust or an institution has been granted registration and subsequently, if the Principal Commissioner or Commissioner of Income-tax is satisfied that the activities of any trust or institution are not genuine or are not being carried out in accordance with the objects of the trust or institution, he can pass an order in writing canceling the registration granted under section 12AA and 12A (as it stood before its amendment by the Finance (No.2) Act, 1996). However, the trust or institution should be given a reasonable opportunity of being heard.

(vii) Any order passed by the Principal Commissioner or Commissioner of Income-tax under section 12AA refusing registration is appealable under section 253 to the Income-tax Appellate Tribunal.

(viii) Where a trust or an institution has been granted registration, and subsequently it is noticed that its activities are being carried out in such a manner that,—

(a) its income does not enure for the benefit of general public;

(b) it is for benefit of any particular religious community or caste;
(c) any income or property of the trust is applied for benefit of specified persons like author of trust, trustees etc.; or

(d) its funds are invested in prohibited modes,

then, the Principal Commissioner or the Commissioner may cancel the registration of such trust or institution. **The Commissioner may also cancel the registration of such trust or institution, if it has not complied with the requirement of any other law and the order, direction or decree, by whatever name called, holding that such non-compliance has occurred, has either not been disputed or has attained finality.** However, if the trust or institution proves that there was a reasonable cause for the activities to be carried out in the above manner, the registration shall not be cancelled.

**ILLUSTRATION 9**

Educare, a trust created with the objective of promoting primary education in rural areas, filed an application for registration under section 12A on 30th April, 2019. Since the application was not disposed of by the Commissioner on or before 31st October, 2019 as required under section 12AA(2), the trust contended that it was deemed to be registered as per the provisions of section 12AA(1). Examine the correctness of contention of the trust.

**SOLUTION**

As per the provisions of section 12AA(2), every order granting or refusing registration under section 12AA(1)(b), **shall** be passed by the registering authority before the expiry of six months from the end of the month in which the application was received under section 12A(1)(a) or section 12A(1)(aa).

The Supreme Court, in *CIT v. Society for Promotion of Education (2016) 382 ITR 6*, held that once an application under section 12AA was made and the same was not responded to within six months, the trust would be deemed as registered with effect from the date following the expiry of the six month period.

Applying the rationale of the above Supreme Court ruling in this case, the trust would be deemed as registered with effect from 1.11.2019. The contention that the trust is deemed to be registered, since its application for registration has not been disposed of within six months is, therefore, correct.

**Note:** The benefit of exemption under section 11 and 12 would be available from the A.Y. 2020-21, being the assessment year relevant to the financial year in which such application is made.

**ILLUSTRATION 10**

A charitable trust, whose income can be exempt under section 11 of the Income-tax Act, 1961, was formed on 1st March, 2017. For the accounting year ended 31st March, 2020, it earned an income of ₹3,60,000.
It filed with the Commissioner of Income-tax its application for registration on 31st August, 2019 explaining that for good and sufficient reasons, it was prevented from filing the application for so long.

Examine -

(i) by which date the application for registration should have been filed;

(ii) whether such an application could have been filed before the formation of the trust;

(iii) in the absence of an order of registration from the Commissioner, can the trust be deemed to be registered;

(iv) the steps to be taken by the trust to secure exemption from income-tax;

(v) whether a certificate of registration once granted can be cancelled and if so, the conditions there for.

SOLUTION

(i) The requirement of filing an application for registration under section 12A within one year of creation of the trust has been removed. The application can be filed at any time now. Accordingly, the provisions of sections 11 and 12 would apply from the assessment year relevant to the financial year in which the application is made i.e. the exemption would be available only with effect from the assessment year relevant to the previous year in which the application was filed.

However, where registration has been granted to the trust under section 12AA and on the said date, assessment proceedings relating to earlier assessment years are pending, then, the benefit of sections 11 and 12 shall be available in respect of income derived from property held under trust in those years, provided the objects and activities of the trust remain unchanged.

(ii) No. The application for registration under section 12A cannot be filed before the formation of the trust.

(iii) As per section 12AA(2), every order granting or refusing registration should be passed before the expiry of 6 months from the end of the month in which the application was received under section 12A. The Supreme Court, in CIT v. Society for Promotion of Education (2016) 382 ITR 6, held that the trust would be deemed as registered if the application under section 12AA is not disposed of within the stipulated period of six months. Therefore, in this case, the trust would be deemed as registered with effect from 1st March, 2020. The benefit of exemption under section 11 and 12 would be available from A.Y. 2020-21, being the assessment year relevant to the financial year in which the application is made.

(iv) The following are the steps to be taken by the trust to secure exemption from income-tax:
(1) The trust should be registered with the Principal Commissioner or Commissioner of Income-tax under section 12AA.

(2) The accounts of the trust for the previous year must be audited by a Chartered Accountant if its total income without giving effect to the provisions of section 11 and section 12 exceeds the maximum amount which is not chargeable to tax. The audit report in the prescribed form, duly signed and verified by the Chartered Accountant, should be furnished along with the return of income of the trust for the relevant assessment year.

(3) At least 85% of the income is required to be applied for the approved purposes.

(4) The unapplied income and the money accumulated or set apart should be invested or deposited in the specified forms or modes, after filing statement in Form 10 on or before the due date of filing return of income specified under section 139(1).

(v) Yes, the certificate of registration can be cancelled by the Commissioner. According to section 12AA, if the Commissioner is satisfied that the activities of the trust are not genuine or are not being carried out in accordance with the objects of the trust, he shall, after giving the trust a reasonable opportunity of being heard, pass an order in writing cancelling the registration of the trust.

Further, section 12AA(4) provides that where a trust or an institution has been granted registration, and subsequently it is noticed that its activities are being carried out in such a manner that,—

(i) its income does not enure for the benefit of general public;

(ii) it is for benefit of any particular religious community or caste;

(iii) any income or property of the trust is applied for benefit of specified persons like author of trust, trustees etc.; or

(iv) its funds are invested in prohibited modes,

then, the Commissioner may cancel the registration of such trust or institution. The Commissioner may also cancel the registration of such trust or institution, if it has not complied with the requirement of any other law and the order, direction or decree, by whatever name called, holding that such non-compliance has occurred, has either not been disputed or has attained finality. However, if the trust or institution proves that there was a reasonable cause for the activities to be carried out in the above manner, the registration shall not be cancelled.
(5) Denial of Exemption [Section 13]

(i) Income not eligible for exemption under sections 11 and 12

(a) Income from property held under a trust for private religious purposes - Where the property is held under a trust for private religious purposes, no part of the income will be exempt if it does not ensure for the benefit of the public [Section 13(1)(a)].

(b) Income from trust established for benefit of any particular religious community or caste - Where a trust has been established for the benefit of any particular religious community or caste, the income thereof will not be eligible for exemption. However, a trust or institution created or established for the benefit of scheduled caste, backward classes, scheduled tribes or women and children shall not be treated as a trust or institution created or established for the benefit of a religious community or caste within the meaning of section 13(1)(b).

(c) Income of trust enuring for the benefit of any person referred to in section 13(3) - Where the trust or the institution has been created or established after 31.3.1962, if any part of its income enures directly or indirectly for the benefit of any person referred to in section 13(3).

Irrespective of the date of the creation of the trust or the establishment of the institution, if any part of its income or any property belonging to it during the relevant previous year is used or applied directly or indirectly for the benefit of any person referred to in section 13(3) [Section 13(1)(c)].

(d) Deposit or investment of funds in impermissible modes - Any income of a trust or institution, if –

(1) its funds are invested or deposited otherwise than in the forms or modes specified in section 11(5);

(2) it holds shares in a company other than -

(i) a public sector company; or

(ii) shares prescribed as a form or mode of investment under section 11(5)(xii).

However, these restrictions do not apply in respect of:

(a) any assets forming part of corpus of the trust as on 1-6-1973.

(b) any accretion to the corpus shares by way of bonus shares allotted to the trust.

(c) debentures issued by or on behalf of any company or corporation and acquired by the trust before March 1, 1983.
d) any asset not covered under section 11(5), where such asset is held for not more than one year from the end of the previous year in which such asset is acquired.

e) any funds representing the profits and gains of business, being profits and gains of any previous year relevant to the assessment year 1984-85 or any subsequent assessment year. However, such relaxation of the restriction will be denied unless the trust keeps separate accounts for the business. As already noted, subject to certain exceptions, such business profits are no longer eligible for exemption under section 11.

(ii) **Prohibited use or application** - We have noted above that when any part of the income or any property of the trust whenever created, is, during the previous year, used or applied directly, for the benefit of any person referred to in section 13(3), the denial of exemption operates. Section 13(2) specifies a few particular instances where the income or the property is to be deemed to have been used for the benefit of a person referred to in section 13(3). It should be noted that those particular instances do not in any way restrict the general meaning of the expression “used or applied for the benefit of a person”. The provisions of section 13(2) are as follows:

The income or the property of the trust or institution or any part of such income or property is to be deemed to have been used or applied for the benefit of a person referred to in section 13(3) in the following cases:

(a) **Loan without adequate interest or adequate security** - If any part of the income or the property of the trust or institution is or continues to be lent to any person referred to in section 13(3) for any period during the previous year without either adequate security or adequate interest or both.

(b) **Allowing use of property without adequate rent** - If any land, building or other property of the trust or institution is or continues to be, made available, for the use of any person referred to in section 13(3) for any period during the previous year without charging adequate rent or other compensation.

(c) **Excess payment for services** - If any amount is paid out of the resources of the trust or institution to any of the persons referred to in section 13(3) for services rendered to the trust or institution but such amount is in excess of a reasonable sum payable for such services.

(d) **Inadequate remuneration for services rendered** - If the services of the trust or institution are made available to any person referred to in section 13(3) without adequate remuneration or other compensation.

(e) **Excess payment for purchase of property** - If any share, security or other property is purchased by or on behalf of the trust or institution from any person referred to in
section 13(3) during the previous year for a consideration which is more than adequate.

(f) **Inadequate consideration for property sold** - If any share, security or other property is sold by or on behalf of the trust or institution to any person referred to in section 13(3) during the previous year for a consideration which is less than adequate.

(g) **Diversion of income or property exceeding ₹ 1,000** - If any income or property of the trust or institution is diverted during the previous year in favour of any person referred to in section 13(3) provided the aggregate value of such income and property diverted exceeds ₹ 1,000.

(h) **Investment in substantial interest concerns** - If any funds of the trust or institution are, or continue to remain, invested for any period during the previous year in any concern in which any person referred to in section 13(3) has a substantial interest.

Section 13(4) provides some respite where the aggregate of the funds invested in the said concern does not exceed five per cent of the capital of that concern. In such a case, the exemption under section 11 will be denied only in relation to such income as arises out of the said investment.

(iii) **Exemption not to be denied to charitable trusts providing educational or medical facilities to specified persons [Section 13(6)]** - A charitable or religious trust running an educational institution or a medical institution or a hospital shall not be denied the benefit of exemption under section 11 merely due to the reason that the benefit of educational or medical facilities have been provided to the specified persons referred to in section 13(3). However, the value of such facilities provided to such specified persons either free of cost or at a concessional rate would be deemed to be the income of the trust. Such income would not be eligible for exemption under section 11.

(iv) **Anonymous donations [Section 13(7)]** - The exemption provisions contained in section 11 or section 12 shall not be applicable in respect of any anonymous donation referred to in section 115BBC on which tax is payable in accordance with the provisions of that section. For example, section 11(1)(d) provides that any income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution shall not be included in the total income of such trust/institution for the relevant previous year.

However, if a trust or institution established wholly for charitable purposes receives an anonymous donation with a specific direction that the donation shall form part of the corpus of the trust or institution, such anonymous donation would not be exempt by virtue of section 11(1)(d). It would be taxable at 30% as provided in section 115BBC.

(v) **Exemption to be denied to a charitable trust having its main object as “advancement of any other object of general public utility” if its trading receipts exceed the specified threshold irrespective of withdrawal of approval or cancellation of registration or rescindment of notification [Section 13(8)]**

(a) Under sections 11 and 12, income of any charitable trust or institution is exempt if
such income is applied for charitable purposes in India and such institution is registered under section 12AA.

(b) The definition of “charitable purpose” under section 2(15) provides that the advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income from such activity, unless,

(1) such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility; and
(2) the aggregate receipts from such activity or activities, during the previous year, does not exceed 20% of the total receipts, of the trust or institution undertaking such activity or activities, for the previous year.

(c) Thus, a charitable trust or institution pursuing “advancement of object of general public utility” may be a charitable trust in one year and not a charitable trust in another year depending on the percentage of receipts from commercial activities vis-à-vis its total receipts.

(d) Therefore, no exemption would be available to a trust or institution for the previous year in which the receipts from commercial activities exceed 20% of the total receipts of that year. However, this temporary excess in one year may not be treated as altering the very nature of the trust or institution so as to lead to cancellation of registration or withdrawal of approval or rescinding of notification issued in respect of trust or institution.

(e) Therefore, there is need to ensure that if the purpose of a trust or institution does not remain charitable in a previous year on account of the commercial receipts exceeding the specified percentage of total receipts, then, such trust or institution would not be entitled to get benefit of exemption in respect of its income for that previous year in which the commercial receipts exceed the specified percentage of total receipts. The denial of exemption would be compulsory by operation of law and would not be dependent on any approval being withdrawn or registration being cancelled or a notification being rescinded.

(f) Accordingly, section 13(8) ensures that such trust and institution does not get benefit of tax exemption under section 11 or 12 in the year in which its receipts from commercial activities exceed the specified percentage of total receipts, whether or not the registration or approval granted or notification issued is cancelled, withdrawn or rescinded in respect of such trust or institution.
Clarification regarding cancellation of registration u/s 12AA of the Income-tax Act, 1961 in certain circumstances [Circular No - 21/2016 dated: May 27, 2016]:

The CBDT has clarified that it shall not be mandatory to cancel the registration already granted u/s 12AA to a charitable institution merely on the ground that the cut-off specified (20% of the total receipts) in the proviso to section 2(15) is exceeded in a particular year without there being any change in the nature of activities of the institution.

If in any particular year, the specified cut-off is exceeded, the tax exemption would be denied to the institution in that year and cancellation of registration would not be mandatory unless such cancellation becomes necessary on the ground(s) prescribed under the Act.

With the introduction of Chapter XII-EB in the Act vide Finance Act, 2016, prescribing special provisions relating to tax on accreted income of certain trusts and institutions, cancellation of registration granted under section 12AA may lead to a charitable institution getting hit by subsection (3) of section 115TD and becoming liable to tax on accreted income. The cancellation of registration without justifiable reasons may, therefore, cause additional hardship to an assessee-institution due to attraction of tax-liability on accreted income. The field authorities are, therefore, advised not to cancel the registration of a charitable institution granted u/s 12AA just because the proviso to section 2(15) comes into play. The process for cancellation of registration is to be initiated strictly in accordance with section 12AA(3) and 12AA(4) after carefully examining the applicability of these provisions.

(vi) **Non-submission of statement in prescribed form on or before the due date of filing return of income under section 139(1) [Section 13(9)]** - In case the statement in Form 10 is not submitted on or before the due date of filing return of income under section 139(1), then, the benefit of accumulation would not be available and such income would be taxable at the applicable rate. Further, the benefit of accumulation would also not be available if return of income is not furnished on or before the due date of filing return of income specified in section 139(1).

(vii) **Prohibited category of persons** - Section 13(3) gives the list of persons, use or application of the income or property of a trust for whose direct or indirect benefit results in a denial of the exemption contemplated in section 11 for a charitable or religious trust or institution. The said persons are:

1. The author of the trust or the founder of the institution.
2. Any person who has made a substantial contribution to the trust or institution, that is, any person whose total contribution up to the end of the relevant previous year exceeds ₹ 50,000.
3. Where the author, founder or the person making a substantial contribution is a HUF, any member of the family.
(4) Any trustee of the trust or manager (by whatever name called) of the institution.

(5) Any relative of any such author, founder, person, member, trustee or manager as referred to above.

(6) Any concern in which any of the persons referred to in clauses (1) to (5) above has a substantial interest.

Relative - The expression “relative”, in relation to an individual, means -

(a) spouse of the individual;
(b) brother or sister of the individual;
(c) brother or sister of the spouse of the individual;
(d) any lineal ascendant or descendant of the individual;
(e) any lineal ascendant or descendant of the spouse of the individual;
(f) spouse of a person referred to in (b), (c), (d) or (e) above;
(g) any lineal descendant of a brother or sister of either the individual or the spouse of the individual;

Substantial interest in a concern - Section 13(2)(h), section 13(3) and section 13(4) refers to cases where a person has a substantial interest in a concern. These references occur where the “Prohibited use or application” and “Prohibited category of persons” have been described. The circumstances in which a person shall be deemed to have a substantial interest in a concern, have been laid down in Explanation 3 to section 13.

Anonymous Donations received by Charitable Trusts/Institutions to be subject to tax [Section 115BBC]

(i) As per the provisions of the Income-tax Act, 1961, tax exemption under section 10(23C) and section 11 are available to certain entities, as briefed in the table below, on fulfillment of the conditions prescribed under the relevant sections –
13.40  DIRECT TAX LAWS

<table>
<thead>
<tr>
<th>Entity</th>
<th>Applicable section</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charitable or religious trusts/institutions</td>
<td>11</td>
</tr>
<tr>
<td>Universities and other educational institutions</td>
<td>10(23C)(iiiad) and (vi)</td>
</tr>
<tr>
<td>Hospitals and other medical institutions</td>
<td>10(23C) (iiiiae) and (viiia)</td>
</tr>
<tr>
<td>Notified funds or institutions established for charitable purposes</td>
<td>10(23C)(iv)</td>
</tr>
<tr>
<td>Notified trusts or institutions established wholly for public religious purposes or wholly for public religious and charitable purposes</td>
<td>10(23C)(v)</td>
</tr>
</tbody>
</table>

(ii) Section 115BBC has been inserted to tax anonymous donations received by the above entities at 30%.

(iii) In order to provide relief to these trusts and institutions and to reduce their compliance burden, an exemption limit has been introduced, and only the anonymous donations in excess of this limit would be subject to tax @30% under section 115BBC.

(iv) The exemption limit is the higher of the following –

(1) 5% of the total donations received by the assessee; or

(2) ₹ 1 lakh.

(v) The total tax payable by such institutions would be –

(1) tax @30% on anonymous donations exceeding the exemption limit as calculated above; and

(2) tax on the balance income i.e. total income as reduced by the anonymous donations which have been subject to tax @30% under section 115BBC.

(vi) The following table illustrates the calculation of anonymous donations liable to tax @30% under section 115BBC –

<table>
<thead>
<tr>
<th>Situation</th>
<th>I</th>
<th>II</th>
<th>III</th>
<th>IV</th>
<th>V</th>
<th>VI</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Total donations during the year (₹)</td>
<td>Anonymous donations received during the year (₹)</td>
<td>Exemption (₹)</td>
<td>Anonymous donations taxable @30% (₹)</td>
<td>Donations subject to tax at normal rates # (₹)</td>
</tr>
<tr>
<td>A</td>
<td></td>
<td>15,00,000</td>
<td>4,00,000</td>
<td>1,00,000</td>
<td>3,00,000</td>
<td>12,00,000</td>
</tr>
<tr>
<td>B</td>
<td></td>
<td>30,00,000</td>
<td>7,00,000</td>
<td>1,50,000</td>
<td>5,50,000</td>
<td>24,50,000</td>
</tr>
<tr>
<td>C</td>
<td></td>
<td>40,00,000</td>
<td>10,00,000</td>
<td>2,00,000</td>
<td>8,00,000</td>
<td>32,00,000</td>
</tr>
</tbody>
</table>

# It is possible to take a view that the remaining donations reflected in Column VI which are taxable at normal rates would be eligible for application of income and thereby, the benefit of exemption under section 11 would apply.
(vii) For this purpose, “anonymous donation” means any voluntary contribution referred to in section 2(24)(iia), where the person receiving such contribution does not maintain a record of the identity indicating the name and address of the person making such contribution and such other particulars as may be prescribed.

(viii) However, the above provision does not apply to a trust or institution created or established wholly for religious purposes.

(ix) Further, anonymous donations to trusts/institutions created or established wholly for religious and charitable purposes (i.e. partly charitable and partly religious institutions/trusts) would be taxed only if such anonymous donation is made with a specific direction that such donation is for any university or other educational institution or any hospital or other medical institution run by such trust or institution. Other anonymous donations received by such trusts/institutions are not taxable.

(x) Section 13(7) provides that the exemption provisions contained in section 11 or section 12 shall not be applicable in respect of any anonymous donation referred to in section 115BBC on which tax is payable in accordance with the provisions of that section.

(xi) For example, section 11(1)(d) provides that any income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution shall not be included in the total income of such trust/institution for the relevant previous year. However, if a trust or institution established wholly for charitable purposes receives an anonymous donation with a specific direction that the donation shall form part of the corpus of the trust or institution, such anonymous donation would not be exempt by virtue of section 11(1)(d). It would be taxable at 30% as provided in section 115BBC.

(xii) Similarly, section 10(23C) provides that any anonymous donation referred to in section 115BBC on which tax is payable in accordance with the provisions of the said section shall be included in the total income. Consequently, sections 10(23C) and 13 provide that any income by way of any anonymous donation which is taxable under the provisions of section 115BBC shall not be excluded from the total income of the trust or institution.

**ILLUSTRATION 11**

The following trusts claim that anonymous donations received by them during the financial year 2019-20 are not liable to tax under section 115BBC:

(i) A charitable trust referred to in section 11 which applied the entire amount of anonymous donations for purposes of the trust during the relevant financial year.

(ii) A trust established wholly for religious purposes which applied 85% of the amount of anonymous donations for the purposes of the objects of the trust during the relevant financial year.

Examine the validity of the claim made by the trusts.
13.42 DIRECT TAX LAWS

SOLUTION

(i) Section 115BBC provides for levy of tax @ 30% on anonymous donation received by, *inter alia*, charitable trusts or institutions referred to in section 11 in the following manner:

(a) the amount of income-tax calculated @30% on the aggregate of anonymous donations received in excess of 5% of the total donations received by the assessee or one lakh rupees, whichever is higher; and

(b) the amount of income-tax with which the assessee would have been chargeable had his total income been reduced by the aggregate of the anonymous donations received in excess of 5% of the total donations received by the assessee or ₹ 1 lakh, as the case may be.

Further, section 13(7) provides that the exemption provisions contained in sections 11 and 12 shall not be applicable in respect of any anonymous donation liable to tax under section 115BBC. As such, application of the anonymous donations received by the charitable trust for charitable purposes does not confer any exemption from tax. Therefore, the claim for non-taxability under section 115BBC of anonymous donations received by the charitable trust is not valid in law.

However, a view may be taken that anonymous donation up to higher of 5% of total donations or ₹ 1 lakh, which is taxable at normal rates would be eligible for application of income and thereby, the benefit of exemption under section 11 would apply.

(ii) Section 115BBC(2) provides that the provisions contained in section 115BBC(1) relating to the taxability of anonymous donations are not applicable to any trust or institution created or established wholly for religious purposes. As such, the trust established wholly for religious purposes is not liable to be taxed in respect of the anonymous donations received by it. Therefore, the claim made by the trust is valid in law. The application or non-application of such anonymous donation for the purposes of trust during the relevant financial year is not germane to the issue of taxability under section 115BBC.

13.4 TAX ON ACCRETED INCOME OF CERTAIN TRUSTS AND INSTITUTIONS [CHAPTER XII-EB]

(1) Background for introduction of Exit Tax

(i) As per section 2(24), "income" includes any voluntary contribution received by a charitable trust or institution or a fund.
(ii) Sections 11 and 12 provide exemption to trusts or institutions in respect of income derived from property held under trust and voluntary contributions, subject to the conditions stipulated thereunder.

(iii) The exemption is subject to the condition that the income derived from property held under trust should be applied for charitable purposes; and where such income cannot be applied during the previous year, it has to be accumulated and invested in the modes prescribed and applied for such purposes in accordance with specified conditions.

(iv) If the accumulated income is not applied in accordance with the conditions provided in the said section within a specified time, then such income is deemed to be taxable income of the trust or the institution. Section 12AA provides for registration of the trust or institution which entitles them to be able to get the benefit of sections 11 and 12. It also provides the circumstances under which the registration can be cancelled. Section 13 of the Act provides for the circumstances under which exemption under section 11 or 12 in respect of whole or part of income would not be available to a trust or institution.

(v) A society or a company or a trust or an institution carrying on charitable activity may –

(1) voluntarily wind up its activities and dissolve; or
(2) merge with any other charitable or non-charitable institution; or
(3) convert into a non-charitable organization.

There is, however, no specific provision in the income-tax law as to how the assets of such a charitable institution should be dealt with.

(vi) Under section 11, certain amount of income of prior period can be brought to tax on failure of certain conditions. However, there is no provision in the Income-tax Act, 1961, which ensure that the corpus and asset base of the trust accreted over a period of time, with promise of it being used for charitable purpose, continues to be utilised for charitable purposes and is not used for any other purpose.

(vii) Consequently, it is always possible for charitable institutions to transfer assets to a non-charitable institution.

(viii) In order to ensure that the benefit conferred over a period of time by way of exemption is not misused and to plug the gap in law that allows the charitable trusts having built up corpus/wealth through exemptions being converted into non-charitable organisation with no tax consequences, Chapter XII-EB imposes additional income-tax in the nature of an exit tax when the organization is converted into a non-charitable organization or gets merged with a non-charitable organization or does not transfer the assets to another charitable organisation.
(2) **Salient Features:**

<table>
<thead>
<tr>
<th>Section</th>
<th>Provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) 115TD(1)</td>
<td><strong>Circumstances where levy of tax on accreted income is attracted:</strong> &lt;br&gt;The accreted income of a trust or institution registered under section 12AA shall be taxable at the maximum marginal rate (@34.944%) on – &lt;br&gt;(1) conversion of the trust or institution into a form not eligible for grant of registration under section 12AA; or &lt;br&gt;(2) merger with an entity not having similar objects and registered under section 12AA; or &lt;br&gt;(3) non-distribution of assets on dissolution to any charitable institution registered under section 12AA or approved under section 10(23C) within a period of 12 months from the end of the month in which the dissolution takes place. &lt;br&gt;This levy of exit tax shall be in addition to income chargeable in the hands of the entity.</td>
</tr>
<tr>
<td>(ii) 115TD(3)</td>
<td><strong>Deemed conversion into non-eligible form - Circumstances:</strong> &lt;br&gt;A trust or an institution shall be deemed to have been converted into any form not eligible for registration under section 12AA in a previous year, if,— &lt;br&gt;(i) the registration granted to it under section 12AA has been cancelled; or &lt;br&gt;(ii) it has adopted or undertaken modification of its objects which do not conform to the conditions of registration and,— &lt;br&gt;(a) it has not applied for fresh registration under section 12AA in the said previous year; or &lt;br&gt;(b) it has filed application for fresh registration under section 12AA but the said application has been rejected.</td>
</tr>
<tr>
<td>(iii) 115TD(2)</td>
<td><strong>Meaning of Accreted Income:</strong> &lt;br&gt;Aggregate FMV of total assets as on the specified date &lt;br&gt;<strong>Less</strong> &lt;br&gt;Total liability computed in accordance with the prescribed method of valuation [See Method of Valuation prescribed by CBDT given at the end of para 13.4]</td>
</tr>
</tbody>
</table>
Notes –

(1) Accreted income attributable to any asset which is established to have been directly acquired by the trust or institution out of its agricultural income exempt under section 10(1) would be ignored. Liability, in relation to such asset, also has to be ignored.

(2) Accreted income attributable to any asset acquired by the trust or institution during the period beginning from the date of its creation or establishment and ending on the date from which the registration under section 12AA became effective, if the trust or institution has not been allowed any benefit of sections 11 and 12 during the said period, would be ignored. Liability, in relation to such asset, also has to be ignored.

(3) The asset and the liability of the charitable organisation which have been transferred on dissolution to another charitable trust or institution registered under section 12AA or a fund/institution/trust/university/educational institution/hospital/medical institution approved under section 10(23C) within specified time have to be ignored while calculating accreted income.

Meaning of specified date [Explanation below section 115TD(7)]:

<table>
<thead>
<tr>
<th>Case</th>
<th>Specified Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) conversion of the trust or institution registered u/s 12AA into a form not eligible for registration u/s 12AA</td>
<td>The date of conversion</td>
</tr>
<tr>
<td>(ii) merger with an entity not having similar objects or not registered u/s 12AA</td>
<td>The date of merger</td>
</tr>
<tr>
<td>(iii) non-distribution of assets on dissolution to any charitable institution registered u/s 12AA or approved u/s 10(23C) within a period twelve months from dissolution.</td>
<td>The date of dissolution</td>
</tr>
</tbody>
</table>

2 Where the benefit under sections 11 and 12 have been allowed to the trust or institution in respect of any previous year or years beginning prior to the date from which the registration under section 12AA became effective, then, the registration shall be deemed to have become effective from the first day of the earliest previous year. Thus, registration under section 12AA shall include any registration obtained under section 12A as it stood before its amendment by the Finance (No.2) Act, 1996.
### Date of conversion [Explanation below section 115TD(7)]:

<table>
<thead>
<tr>
<th>Case</th>
<th>Specified Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Where the registration granted to it u/s 12AA has been cancelled</td>
<td>The date of the order cancelling registration u/s 12AA</td>
</tr>
<tr>
<td>(ii) Where it has adopted or undertaken modification of its objects which do not conform to the conditions of registration and has not made an application for fresh registration or the application made has been rejected.</td>
<td>The date of adoption or modification of any object.</td>
</tr>
</tbody>
</table>

### Exit tax payable even if no income-tax is payable by the Trust/Institution:

Even if no income-tax is payable by the trust or institution on its total income, tax on accreted income shall be payable by the trust or institution, like any other additional income-tax.

### Period within which tax on accreted income has to be paid to the credit of the Central Government:

The principal officer or the trustee of the trust or the institution, as the case may be, and the trust or the institution shall also be liable to pay the tax on accreted income to the credit of the Central Government within fourteen days from,—

<table>
<thead>
<tr>
<th>Circumstance</th>
<th>Relevant date</th>
</tr>
</thead>
</table>
| (1) Where the registration granted u/s 12AA has been cancelled             | the date on which –
<p>|                                                                            | (a) the period for filing appeal under section 253 against the order rejecting the application expires and no appeal has been filed by the trust or the institution; (or) |
|                                                                            | (b) the order in any appeal, confirming the cancellation of the application, is received by the trust or the institution |
| (2) Where the trust has modified its objects and has not applied for fresh registration u/s 12AA | the end of the previous year |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
</table>
| (3) | Where the trust has modified its objects and has filed application for fresh registration u/s 12AA, but the same was rejected | the date on which –
|   |   | (a) the period for filing appeal under section 253 against the order rejecting the application expires and no appeal has been filed by the trust or institution; (or)
|   |   | (b) the order in any appeal, confirming the cancellation of the application, is received by the trust or the institution |
| (4) | Where trust has merged with an entity not having similar objects or not registered u/s 12AA | the date of merger |
| (5) | Where the trust fails to transfer upon dissolution all its assets to another registered trust or institution or approved fund or institution within 12 months from the end of the month in which the dissolution takes place | the date on which the period of 12 months expires. |
| (vi) | 115TD(6) | No credit available for tax paid on accreted income:
The tax on accreted income shall be final tax for which no credit can be taken by the trust or institution or any other person. |
| (vii) | 115TD(7) | Non-availability of deduction under any other provision of the Act:
No deduction is allowable under any other provision of the Act to the trust or institution or any other person in respect of the income which has been charged to tax or the tax thereon. |
| (viii) | 115TE | Interest for non-payment of tax within prescribed time:
In case of failure of payment of tax within the prescribed time, a simple interest@1% p.m. or part of it shall be applicable for the period of non-payment. |
13.48

DIRECT TAX LAWS

<table>
<thead>
<tr>
<th>Period of non-payment:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Beginning from</strong></td>
<td><strong>Ending with</strong></td>
</tr>
</tbody>
</table>
| The date immediately after the last date on which such tax was payable | The date on which the tax is actually paid.

(ix) 115TF

**Circumstance when trust or institution is deemed to be assessee-in-default:**

The principal officer or the trustee and the trust or the institution shall be deemed to be assessee-in-default for non-payment of tax and all provisions related to the recovery of taxes shall apply. Further, in the case of transfer of assets upon dissolution of the trust or institution to a recipient, which is not a charitable organisation, the recipient of assets of the trust shall also be liable to be held as assessee-in-default in case of non-payment of tax and interest. However, in such a case, the recipient's liability shall be limited to the extent to which the assets received by him is capable of meeting the liability.

**Note** - As per section 115TD(2), “Accreted Income” means the aggregate FMV of total assets as on the specified date less total liability computed in accordance with the prescribed method of valuation. Accordingly, the CBDT has inserted Rule 17CB from 1.6.2016 providing for method of valuation of assets and liabilities.

**Method of valuation for the purposes of sub-section (2) of section 115TD**

<table>
<thead>
<tr>
<th>Rule</th>
<th>Provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>The aggregate fair market value of the total assets of the trust or institution, shall be the aggregate of the fair market value of all the assets in the balance sheet as reduced by—</td>
</tr>
<tr>
<td></td>
<td>(i) any amount of income-tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of income-tax claimed as refund under the Act, and</td>
</tr>
<tr>
<td></td>
<td>(ii) any amount shown as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset.</td>
</tr>
</tbody>
</table>

(2) The fair market value of the asset shall be determined in the following manner, namely -

**(I) Shares and securities**

<table>
<thead>
<tr>
<th>(a) Quoted shares and securities</th>
<th>(i) the average of the lowest and highest price of such shares and securities quoted on a recognised stock exchange as on the specified date; or</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i)</td>
<td>(ii) where on the specified date, there is no</td>
</tr>
</tbody>
</table>
trading in such shares and securities on a recognised stock exchange, the average of the lowest and highest price of such shares and securities on a recognised stock exchange on a date immediately preceding the specified date when such shares and securities were traded on a recognised stock exchange,

<table>
<thead>
<tr>
<th>(b)</th>
<th>Unquoted equity shares</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>((A+B - L) \times \frac{PV}{PE})</td>
</tr>
</tbody>
</table>

where,

\(A\) = book value of all the assets in the balance sheet (other than bullion, jewellery, precious stone, artistic work, shares, securities, and immovable property) as reduced by-

(i) any amount of income-tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of income-tax claimed as refund under the Act; and

(ii) any amount shown in the balance sheet as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset;

\(B\) = fair market value of bullion, jewellery, precious stone, artistic work, shares, securities and immovable property as determined in the manner provided in this rule;

\(L\) = book value of liabilities shown in the balance sheet, but not including the following amounts, namely: —

(i) representing contingent liabilities other than arrears of dividends payable in respect of the paid-up capital in respect of equity shares;

(ii) the amount set apart for payment of dividends on preference shares and equity shares;

(iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation;

(iv) any amount representing provision for taxation, other than amount of income-tax paid as deduction.
or collection at source or as advance tax payment as reduced by the amount of income-tax claimed as refund under the Act, to the extent of the excess over the tax payable with reference to the book profits in accordance with the law applicable thereto;

(v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;

(vi) any amount of cumulative preference shares;

PE = total amount of paid up equity share capital as shown in the balance-sheet;

PV = the paid up value of such equity share.

### Shares and securities other than equity shares

The fair market value of shares and securities other than equity shares shall be estimated to be price it would fetch if sold in the open market on the specified date on the basis of the valuation report from a merchant banker or an accountant in respect of such valuation.

### II. Immovable property

The fair market value of an immovable property shall be higher of the following:

(a) price that the property shall ordinarily fetch if sold in the open market on the specified date on the basis of the valuation report from a registered valuer; and

(b) stamp duty value as on the specified date.

### III. A business undertaking

The fair market value of a business undertaking, held by a trust or institution, shall be its net assets determined in accordance with the following formula:

\[
\text{Fair market value} = (A + B - L),\]

The value of A, B and L would be determined in the same manner as discussed above in the case of unquoted equity shares.

### IV. Any other asset

The fair market value of any asset, other than those referred to in (I), (II) and (III), shall be the price that the asset shall ordinarily fetch if sold in the open market on the specified date on the basis of valuation report from a registered valuer.

However, in case no valuer is registered for valuation of such assets, the valuation report shall be obtained from a valuer who is a member of any...
one of the professional valuer bodies viz. Institution of Valuers, Institution of Surveyors (Valuation Branch), Institution of Government Approved Valuers, Practicing Valuers Association of India, the Indian Institution of Valuers, Centre for Valuation Studies, Research and Training, Royal institute of Chartered Surveyors; India Chapter, American Society of Appraisers, USA; Appraisal institute, USA or a valuer who is appointed by any public sector bank or public sector undertakings for valuation purposes.

(3) The total liability of the trust or institution shall be the book value of liabilities in the balance sheet on the specified date but not including the following amounts, namely -

(i) capital fund or accumulated funds or corpus, by whatever name called;
(ii) reserves or surpluses or excess of income over expenditure, by whatever name called;
(iii) any amount representing contingent liability;
(iv) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;
(v) any amount representing provision for taxation, other than the amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of income-tax claimed as refund under the Act, to the extent of the excess over the income-tax payable with reference to the income in accordance with the law applicable thereto.

### Explanation

#### Meaning of certain terms

<table>
<thead>
<tr>
<th>Term</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accountant</td>
<td>A fellow of the Institute of Chartered Accountants of India within the meaning of the Chartered Accountants Act, 1949 who is not appointed by the trust or institution as an auditor;</td>
</tr>
<tr>
<td>Balance sheet</td>
<td>The Balance Sheet of such trust or institution (including the notes annexed thereto and forming part of the accounts) as drawn up on the specified date which has been audited by an accountant.</td>
</tr>
<tr>
<td>Quoted share or security</td>
<td>A share or security quoted on any recognised stock exchange with regularity from time to time, where the quotations of such shares or securities are based on current transaction made in the ordinary course of business;</td>
</tr>
</tbody>
</table>
13.52 DIRECT TAX LAWS

The date referred to in Explanation to section 115TD of the Act.

Meaning of specified date [Explanation below section 115TD]:

<table>
<thead>
<tr>
<th>Case</th>
<th>Specified Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Conversion of the trust or institution registered u/s 12AA into a form not eligible for registration u/s 12AA</td>
<td>The date of conversion</td>
</tr>
<tr>
<td>(ii) merger with an entity not having similar objects or not registered u/s 12AA</td>
<td>The date of merger</td>
</tr>
<tr>
<td>(iii) non-distribution of assets on dissolution to any charitable institution registered u/s 12AA or approved u/s 10(23C) within a period twelve months from dissolution</td>
<td>The date of dissolution</td>
</tr>
</tbody>
</table>

Stamp duty value

The value adopted or assessed or assessable by any authority of the Central Government or a State Government for the purpose of payment of stamp duty in respect of an immovable property.

Unquoted share and security

Share or security which is not a quoted share or security.

13.5 EXEMPTION TO POLITICAL PARTIES [SECTION 13A]

Section 13A of the Income-tax Act, 1961 grants exemption from tax to political parties in respect of their income specified below:

- Income from house property
- Income from other sources
- Capital Gains
- Voluntary contributions received

The aforesaid categories of income would qualify for exemption provided additional conditions for availing the benefit of the said section which are as under are met:

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For the purposes of this section, “political party” means a political party registered under section 29A of the Representation of the People Act, 1951.

ILLUSTRATION 12

Explain in the context of provisions of the Act, whether the income derived during the year ended on 31.03.2020 in following case shall be subject to tax in the A.Y. 2020-21:

A political party, duly registered under section 29A of the Representation of the People Act, 1951, received rent of ₹1,25,000 per month of one of its building let out to a bank from 01.06.2019.

SOLUTION

Rent received by the political party from the bank is an income chargeable under the head "Income from house property". However, according to the provisions of section 13A, income from, *inter alia*, house property shall not be included in total income of a political party registered under section 29A of the Representation of the People Act, 1951, provided the political party fulfils the conditions as specified therein including furnishing a return of income for the previous year in accordance with the provisions of section 139(4B) on or before the due date under section 139. Therefore, if the stipulated conditions are fulfilled by the political party, rent of ₹1,25,000 per month received by the registered political party from letting out of its building to a bank would not be included in its total income.
**13.6 EXEMPTION FOR VOLUNTARY CONTRIBUTIONS RECEIVED BY ELECTORAL TRUSTS [SECTION 13B]**

(1) Any voluntary contribution received by an electoral trust (as may be approved by the CBDT in accordance with the scheme to be made by the Central Government) shall be treated as its income under section 2(24), but shall be exempt under section 13B, if the trust distributes to a registered political party during the year, 95% of the aggregate donations received by it during the year along with the surplus if any, brought forward from any earlier previous year.

(2) Another condition for availing the benefit under this section is that the electoral trust should function in accordance with the rules made by the Central Government. Accordingly, the Central Government has notified Rule 17CA which provides that the following shall be the functions of an electoral trust referred to in section 13B –

(i) The electoral trust may receive voluntary contributions from

(a) an individual who is a citizen of India;
(b) a company which is registered in India; and
(c) a firm or Hindu undivided family or an Association of persons or a body of individuals, resident in India.

(ii) A receipt indicating the following shall be issued by the trust immediately on receipt of any contribution indicating the following:

(a) name and address of the contributor;
(b) Permanent account number of the contributor or passport number in the case of a citizen who is not a resident;
(c) amount and mode of contribution including name and branch of the Bank and date of receipt of such contribution;
(d) name of the electoral trust;
(e) Permanent account number of the electoral trust;
(f) date and number of approval by the prescribed authority; and
(g) Name and designation of the person issuing the receipt.

(iii) The electoral trust shall not accept contributions-

(a) from an individual who is not a citizen of India or from any foreign entity whether incorporated or not;
(b) from any other electoral trust which has been registered as a company under section 25 of the Companies Act, 1956\(^3\) and approved as an electoral trust under the Electoral Trusts Scheme, 2013;

(c) from a Government company as defined in section 2(45) of the Companies Act, 2013; and

(d) from a foreign source as defined in section 2(j) of the Foreign Contribution (Regulation) Act, 2010.

(iv) The electoral trust shall accept contributions only by way of an account payee cheque drawn on a bank or account payee bank draft or by electronic transfer to its bank account and shall not accept any contribution in cash.

(v) The electoral trust shall not accept any contribution without the PAN of the contributor, who is a resident and the passport number in the case of a citizen of India, who is not a resident.

(vi) A political party registered under section 29A of the Representation of the People Act, 1951 shall be an eligible political party and an electoral trust shall distribute funds only to the eligible political parties.

(vii) (a) The electoral trust may, for the purposes of managing its affairs, spend up to 5% of the total contributions received in a year subject to an aggregate limit of `5 lakh in the first year of incorporation and `3 lakh in subsequent years;

(b) the total contributions received in any financial year along with the surplus from any earlier financial year, if any, as reduced by the amount spent on managing its affairs, shall be the distributable contributions for the financial year;

(c) an electoral trust shall be required to distribute the distributable contributions received in a financial year, referred to in item (ii), to the eligible political parties before 31\(^{st}\) March of the said financial year, subject to the condition that at least 95% of the total contributions received during the financial year along with the surplus brought forward from earlier financial year, if any, are distributed.

(viii) The trust shall obtain a receipt from the eligible political party indicating the name of the political party, its permanent account number, registration number, amount of fund received from the trust, date of the receipt and name and designation of person signing such receipt.

\(^3\) Section 8 of the Companies Act, 2013
(ix) The electoral trust shall not utilize any contributions for the direct or indirect benefit of the members or contributors, or for any of the following persons, namely:

(a) the members (including members of its Executive Committee, Governing Committee or Board of Directors) of the electoral trust;
(b) any relative of such Members;
(c) where such member or contributor is a Hindu undivided family, a member of that Hindu undivided family;
(d) any person who has made a contribution to the trust;
(e) any person referred in section 13(3); and
(f) any concern in which any of the persons referred to in clauses (a), (b), (c), (d) and (e) has a substantial interest.

(x) (a) An electoral trust shall keep and maintain such books of account and other documents in respect of its receipts, distributions and expenditure as may enable the computation of its total income in accordance with the provisions of the Act;
(b) The electoral trust shall also maintain a list of persons from whom contributions have been received and to whom the same have been distributed, containing the name, address and permanent account number (PAN) of each such person along with the details of the amount and mode of its payment including the name and branch of the bank.

(xi) Every electoral trust shall get its accounts audited by an accountant as defined in the Explanation below section 288(2) and furnish the audit report in Form No.10BC along with particulars forming part of its Annexure, to the Commissioner of Income-tax or the Director of Income-tax, as the case may be, having jurisdiction over the electoral trust, on or before the due date specified for furnishing the return of income by a company under section 139.

(xii) An electoral trust shall maintain a regular record of proceedings of all meetings and decisions taken therein.

(xiii) Every electoral trust shall furnish a certified copy of list of contributors and a list of political parties, to whom sums were distributed in the manner prescribed in (vii) above, to the Commissioner of Income-tax or the Director of Income-tax, as the case may be, every year along with the audit report;

(xiv) Any change in the shareholders, subsequent to the approval granted under the Electoral Trusts Scheme, 2013 shall be intimated to the Board within thirty days of such change.
Section 2(22AAA) defines ‘Electoral Trust’ to mean a trust so approved by the CBDT, in accordance with the scheme made in this regard by the Central Government.

In exercise of the powers conferred by section 2(22AAA), the Central Government, has through Notification No. 9/2013 dated 31.1.2013, notified the Electoral Trusts Scheme, 2013 to lay down the procedure for grant of approval to an electoral trust which will receive voluntary contributions and distribute the same to political parties.

**Eligibility**

A company registered for the purposes of section 25 of the Companies Act, 1956 satisfying all of the following conditions shall be eligible to make an application for approval as an electoral trust, namely –

1. The company should be registered on or after 1.4.2012 for the purposes of section 25 of the Companies Act, 1956;
2. The name of the company registered for the purposes of section 25 of the Companies Act, 1956 has to include the phrase “electoral trust”;
3. The sole object of the electoral trust should be to distribute the contributions received by it to the political party, registered under section 29A of the Representation of the People Act, 1951;
4. The electoral trust should have a permanent account number.

**Criteria for Approval**

An electoral trust shall be considered for approval if it fulfills all of the following conditions, namely –

1. The company registered for the purposes of section 25 of the Companies Act, 1956, which satisfies the above conditions;
2. The object of the electoral trust shall not be to earn any profit or pass any direct or indirect benefit to its members or contributors, or to any person referred to in section 13(3) or any person referred to in Rule 17CA(10) of the Rules;
3. It has made adequate arrangement for recording the receipts from the contributors in accordance with Rule 17CA;
4. The stipulations contained in Rule 17CA for functioning of the electoral trust are specifically included in the articles of association of the company registered for the purposes of section 25 of the Companies Act, 1956.

**Renewal of approval**

1. The approval shall be valid for the assessment year relevant to the financial year in which such application has been made and for a further period, not exceeding three assessment years, as may be specified in the approval.
2. The electoral trust may apply for renewal of approval at any time during the financial year immediately preceding the last assessment year, for which the approval has been originally granted, and such renewal of approval may be granted after examining the application in the same manner as laid out for approval in this scheme.

Withdrawal of approval

1. The CBDT may withdraw the approval granted under this Scheme if it is satisfied that the electoral trust has ceased its activities or its activities are not genuine or are not carried out in accordance with all or any of the conditions laid down under this Scheme or the provisions of Rule 17CA of the Rules, or any other condition imposed in the approval granted.

2. In order to ascertain whether an electoral trust, after its approval, is functioning in accordance with the provisions of Rule 17CA of the Rules, the CBDT may call for information or documents as it may deem fit from the electoral trust or may get an enquiry conducted in this regard by an income-tax authority or any other agency.

3. If the Commissioner of Income-tax or the Director of Income-tax is satisfied that an approved electoral trust is not fulfilling any of the conditions specified under this Scheme or the conditions subject to which approval was granted to it or does not function in accordance with Rule 17CA, he may, after making appropriate enquiries, furnish a report to the CBDT in this regard and the Board may take such action on the report as it may deem fit.

4. An order for withdrawal of the approval shall be passed after giving the electoral trust an opportunity of being heard, and shall record the reasons in writing for the withdrawal of approval.

5. A copy of the order withdrawing the approval shall be sent to the applicant, the Assessing Officer and the Commissioner of Income-tax or the Director of Income-tax, as the case may be.

ILLUSTRATION 13

The books of account maintained by a National Political Party registered with Election Commission for the year ended on 31.3.2020 discloses the following receipts:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Rent of property let out to a departmental store at Chennai</td>
<td>₹6,00,000</td>
</tr>
<tr>
<td>(b) Interest on deposits other than banks</td>
<td>₹5,00,000</td>
</tr>
<tr>
<td>(c) Contribution from 100 persons (who have secreted their names) of ₹21,000 each</td>
<td>₹21,00,000</td>
</tr>
<tr>
<td>(d) Contribution from 10 persons by way of electoral bonds of ₹25,000 each</td>
<td>₹2,50,000</td>
</tr>
</tbody>
</table>
CHARITABLE OR RELIGIOUS TRUSTS AND INSTITUTIONS,
POLITICAL PARTIES AND ELECTORAL TRUSTS

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>(e) Cash contribution @ ₹ 2,100 each from 1,000 members (recorded in books of account)</td>
<td>21,00,000</td>
</tr>
<tr>
<td>(f) Net profit of cafeteria run in the premises at Delhi</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

Compute the total income of the political party for the assessment year 2020-21, with reasons for inclusion or otherwise.

**SOLUTION**

The total income of a political party registered with the Election Commission is to be computed as per section 13A under which the income derived from house property, income from other sources and income by way of voluntary contributions received from any person, on fulfilling of the conditions as mentioned thereunder, are exempt from tax. However, in this case, since cash contribution in excess of ₹ 2,000 is received from 1000 persons, the political party has violated the condition of receipt of donation through account payee cheque/draft or prescribed electronic modes. Further, the political party has also violated the condition of maintenance of records in case of donations exceeding ₹ 20,000 received otherwise than by way of electoral bonds. Hence, its total income has to be computed as under without providing for exemption available under section 13A:

**Computation of total income of National Political Party**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) The rent of the property of ₹ 6 lacs located at Chennai [assuming the same to be the Gross Annual Value] less 30% of Rs.6 lacs, being deduction u/s 24</td>
<td>4,20,000</td>
</tr>
<tr>
<td>(b) Interest received on deposits</td>
<td>5,00,000</td>
</tr>
<tr>
<td>(c) Contribution from 100 persons (who have secreted their names) of ₹ 21,000 each</td>
<td>21,00,000</td>
</tr>
<tr>
<td>(d) Contribution from 10 persons by way of electoral bonds of ₹ 25,000 each</td>
<td>2,50,000</td>
</tr>
<tr>
<td>(e) Cash contribution @ ₹ 2,100 each from 1,000 members (recorded in books of account)</td>
<td>21,00,000</td>
</tr>
<tr>
<td>(f) Net profit of cafeteria at Delhi</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

**Total Income** 56,70,000

**Note** – Alternatively, the political party can contend that only ₹ 45 lakh is taxable on account of non-maintenance of records and receipt of cash donations, in which case the total income would be computed as under:

**Computation of total income of National Political Party**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Rent of the property of ₹ 6 lacs located at Chennai</td>
<td>Exempt</td>
</tr>
<tr>
<td>(b) Interest received on deposits</td>
<td>Exempt</td>
</tr>
</tbody>
</table>

© The Institute of Chartered Accountants of India
Contribution from 100 persons (who have secreted their names) of ₹ 21,000 each  | ₹ 21,00,000
Contribution from 10 persons by way of electoral bonds of ₹ 25,000 each  | Exempt
Cash contribution @ ₹ 2,100 each from 1,000 members (recorded in books of account)  | ₹ 21,00,000
Net profit of cafeteria at Delhi  | ₹ 3,00,000

**Total Income**  | **₹ 45,00,000**

**Note:** It is presumed that the conditions regarding maintenance of books of account, audit, submission of report under section 29C of the Representation of the People Act, 1951 and filing of return of income under section 139(4B) are fulfilled by the political party, and hence it is eligible for exemption of income under section 13A.
EXERCISE

Question 1

A trust, unless created for "charitable purpose", does not qualify to claim exemption under Chapter III of the Act. In this context, explain the meaning of "charitable purpose" and examine whether the following objects constitute part of it:

(i) Rural reconstruction and upliftment of the masses through Cottage Industry.

(ii) Welfare of industrial workers with a stipulation that the workers of settlor of trust have got preference over others.

Answer

Section 2(15) defines “charitable purpose” to include relief of the poor, education, medical relief, yoga, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest and the advancement of any other object of general public utility. However, “advancement of any other object of general public utility” would not be a charitable purpose, if it involves carrying on of any activity in the nature of trade, commerce or business or, any activity of rendering of any service in relation to any trade, commerce or business, for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity or the retention of such income, by the concerned entity.

“Advancement of any other object of general public utility” would continue to be a “charitable purpose”, if the total receipt from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed 20% of the total receipts of the trust in the previous year, and such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility.

(i) The Supreme Court has, in Thiagarajar Charities vs. Addl. CIT (1997) 225 ITR 1010, observed that “cottage industry” is associated with the idea of a small, simple enterprise or industry in which employees work in their own houses or in a small place, gathered together for the purpose, using their own equipments and is usually found in rural areas or so carried on, by the poorer section of the society. In substance, the activity of rural reconstruction and upliftment of masses through cottage industry is to afford relief to the poor and consequently, it is for charitable purpose.

(ii) The welfare of industrial workers with a stipulation that the workers of settlor of trust have preference over others would also constitute “charitable purpose” within the meaning of section 2(15). The Patna High Court has, in CIT v. Tata Steel Charitable Trust (1993) 203 ITR 764, observed that exemption under section 11(1) can be availed only if the following conditions are satisfied –

(1) the trust is created for a charitable purpose; and
(2) no part of the income of such trust enures or has been used or applied directly or indirectly for the benefit of any person referred to in section 13(3).

The list of persons contained in section 13(3) does not include employees of the settlor of the trust. Section 13(3)(d), which includes any relative of the author, can have no application because “relative” means a person connected by birth or marriage with another person. A person having relationship pursuant to a contract like that of an employer and an employee cannot be said to be a relative. The High Court concluded that it was immaterial that any employee of the settler of the trust had acquired any benefit out of the income of the trust as an ordinary member of the community. Therefore, the application of part of the income of the trust for the benefit of the employees of the settler cannot disentitle the trust from claiming exemption under section 11.

Question 2

How do you deal with the following situation? Give reasons for your answer.

Ramji Charitable Trust has filed return of income for the Assessment Year 2020-21 within the stipulated time under section 139(1) and applied only 50% of its income for specified purposes. It intends to accumulate the balance 35% of income to be spent in future years. While completing the assessment, the Assessing Officer disallowed the accumulated income of 35% and taxed the same on the ground that the trust has not made any application under section 11(2) along with return of income. Discuss the validity of the action of the Assessing Officer in this case.

Answer

Section 11(2) provides that a charitable trust has to apply 85% of its income to charitable purposes and where 85% of its income is not applied for such purposes, the trust may accumulate or set apart either the whole or part of its income for future application for such purposes in India. The requirement of the Act is that the trust has to make an application/intimation in the prescribed form, for accumulation of income, specifying the purpose and the period (not exceeding 5 years). The application should be filed or furnished before the assessing authority on or before the due date specified under section 139(1). Further, the money so set apart or accumulated should be invested/deposited in any one or more of these modes or forms specified under section 11(5).

Thus, this requirement of filing application is mandatory and without those particulars, the assessing authority cannot entertain the claim of the assessee under section 11. In case the statement in Form 10 is not submitted on or before the due date of filing return of income under section 139(1), then, the benefit of accumulation would not be available and such income would be taxable at the applicable rate. Further, the benefit of accumulation would also not be available if return of income is not furnished on or before the due date of filing of return of income under section 139(1). Therefore, the action of the Assessing Officer in this case is valid.
Question 3

An institution operating for promotion of education claiming exemption under section 11 since 1994 furnishes the following data for the assessment year 2020-21:

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Particulars</th>
<th>₹ in crores</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i)</td>
<td>Fees collected from students</td>
<td>14</td>
</tr>
<tr>
<td>(ii)</td>
<td>Construction of a new computer science laboratory</td>
<td>0.50</td>
</tr>
<tr>
<td>(iii)</td>
<td>Land acquired to be used as a cricket field for the students</td>
<td>2</td>
</tr>
<tr>
<td>(iv)</td>
<td>Amount earmarked and set apart for construction of an arts block within the next 4 years.</td>
<td>4</td>
</tr>
</tbody>
</table>

Compute the total income of the institution for the A.Y.2020-21.

Answer

**Computation of total income of the institution for the A.Y. 2020-21**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹ (in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fees received</td>
<td>14.00</td>
</tr>
<tr>
<td>Less : 15% (exempt even if not spent for the objects of the institution)</td>
<td>2.10</td>
</tr>
<tr>
<td></td>
<td>11.90</td>
</tr>
<tr>
<td>Less : Accumulated for specified purpose <em>(See Note 2)</em></td>
<td>4.00</td>
</tr>
<tr>
<td>Balance to be spent</td>
<td>7.90</td>
</tr>
<tr>
<td>Actual amount spent on construction of computer science lab <em>(See Note 1)</em></td>
<td>0.50</td>
</tr>
<tr>
<td>Actual amount spent on purchase of land for cricket field <em>(See Note 1)</em></td>
<td>2.00</td>
</tr>
<tr>
<td><strong>Total Income</strong></td>
<td><strong>5.40</strong></td>
</tr>
</tbody>
</table>

Notes:

1. The institution must utilise 85% of its income within the previous year for the objects of the institution. The institution can apply its income either for revenue expenditure or for capital expenditure provided the expenditure is incurred for promoting the objects of the institution. Land acquired and meant for use as cricket field for students is a capital expenditure incurred for promoting the objects of the institution and hence, eligible for deduction. Likewise, the amount spent on construction of computer science laboratory is also eligible for deduction.

2. Section 11(2) provides that a trust/institution can accumulate or set apart its income for a specified purpose by furnishing statement in prescribed format to the concerned Assessing Officer. However, the period for which the funds can be accumulated cannot exceed 5 years.
years. The amount so accumulated should be invested in the specified forms and modes. In this case, the institution has to furnish statement in Form 10 on or before the due date of filing return of income to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is being accumulated or set apart, which shall, in no case, exceed five years. Further, the institution has to invest ₹ 4 crore in the specified forms and modes.

**Question 4**

A public charitable trust registered under section 12AA, for the previous year ending 31.3.2020, derived gross income of ₹ 21 lakhs, which consists of the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>₹ (in Lacs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Income from properties held by trust (net)</td>
<td>10</td>
</tr>
<tr>
<td>(b) Income (net) from business (incidental to main objects)</td>
<td>4</td>
</tr>
<tr>
<td>(c) Voluntary contributions from public</td>
<td>7</td>
</tr>
</tbody>
</table>

The trust applied a sum of ₹ 11.60 lakhs towards charitable purposes during the year which includes repayment of loan taken for construction of orphanage ₹ 3.60 lakhs.

**Determine the taxable income of the trust for the assessment year 2020-21.**

**Answer**

**Computation of taxable income of public charitable trust**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Income from property held under trust (net)</td>
<td>10,00,000</td>
</tr>
<tr>
<td>(ii) Income (net) from business (incidental to main objects)</td>
<td>4,00,000</td>
</tr>
<tr>
<td>(iii) Voluntary contributions from public</td>
<td>7,00,000</td>
</tr>
</tbody>
</table>

Voluntary contribution made with a specific direction towards corpus are alone to be excluded under section 11(1)(d). In this case, there is no such direction and hence, included.

Less: 15% of the income eligible for retention / accumulation without any conditions

<table>
<thead>
<tr>
<th>₹</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>3,15,000</td>
<td></td>
</tr>
</tbody>
</table>

Less: Amount applied for the objects of the trust

<table>
<thead>
<tr>
<th>₹</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>8,00,000</td>
<td></td>
</tr>
<tr>
<td>3,60,000</td>
<td></td>
</tr>
</tbody>
</table>

**Taxable Income**

<table>
<thead>
<tr>
<th>₹</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>6,25,000</td>
<td></td>
</tr>
</tbody>
</table>
Question 5

A charitable trust registered under section 12AA of the Income-tax Act, 1961 has, out of its income of ₹3,90,000 for the year ending 31.3.2020 and sale proceeds of a capital asset, held by it for less than 24 months, amounting to ₹9,60,000, purchased a building during the year ending 31.3.2020 for ₹13,50,000. The capital asset was sold during the year ending 31.3.2020. The building is held only for charitable purposes. The trust claims that the purchase of the building amounts to application of its income for charitable purposes and that the capital gain arising on the sale of the capital asset is deemed to have been applied to charitable purposes. Is the claim made by the charitable trust valid in law?

Answer

Section 11(1)(a) stipulates that in order to avail exemption of income derived from property held under trust wholly for charitable or religious purposes, the trust is required to apply for charitable or religious purposes, 85% of its income from such property. In this case, the trust has earned income of ₹3,90,000 for the year ended 31.3.2020. It has also earned short term capital gain from sale of capital asset for ₹9,60,000. The trust had utilized the entire amount of ₹13,50,000 for the purchase of a building meant for charitable purposes.

The Supreme Court, in S.R.M. M. CT. M. Tiruppani Trust v. CIT (1998) 230 ITR 636, ruled that the assessee-trust, which applied its income for charitable purposes by purchasing a building for use as a hospital, was entitled to exemption under section 11(1) in respect of such income.

The ratio of the decision squarely applies to the case of the charitable trust in question. Therefore, the charitable trust is justified in claiming that the purchase of the building amounted to application of its income for charitable purposes.

Under section 11(1A), where the whole of the sale proceeds of a capital asset held by a charitable trust is utilised by it for acquiring another capital asset, the capital gain arising therefrom is deemed to have been applied to charitable purposes and would be exempt. Section 11(1A) does not make any distinction between a long-term capital asset and a short-term capital asset. The claim of the charitable trust to the effect that the capital gain is deemed to have been applied to charitable purposes is tenable in law.

Question 6

Work out, from the following particulars, the amount of capital gain which shall be deemed to have been applied for charitable or religious purpose arising out of sale of a capital asset utilized for the purposes of trust to the extent of 60%:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of transferred asset</td>
<td>2,40,000</td>
</tr>
<tr>
<td>Sale consideration</td>
<td>3,60,000</td>
</tr>
<tr>
<td>Cost of new asset purchased</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>
Answer

In this case, since the asset which is transferred is utilized for the purposes of the trust only to the extent of 60%, only the proportionate amount (i.e. 60%) of the capital gain would be regarded as having been applied for charitable or religious purposes.

As per section 11(1A), where a capital asset held under trust is transferred, and only a part of the net consideration is utilized for acquiring a new capital asset, only so much of the capital gain as is equal to the amount, if any, by which the amount so utilized exceeds the cost of the transferred asset shall be considered to have been applied for the objects of the trust.

In this case, only a part of the net consideration of ₹ 3,60,000 is utilized for acquiring the new capital asset costing ₹ 3,00,000. The amount utilized in acquiring the new asset (i.e. ₹ 3,00,000) exceeds the cost of the transferred asset (i.e. ₹ 2,40,000) by ₹ 60,000.

Therefore, only 60% of (₹ 3,00,000 – ₹ 2,40,000) = 60% of ₹ 60,000 = ₹ 36,000 is deemed to be applied for the objects of the trust.

Question 7

An electoral trust approved by the CBDT is not liable to income-tax in respect of voluntary contribution received and other income - Examine the correctness of the statement.

Answer

Section 13B provides exemption in respect of voluntary contribution received by an electoral trust approved by the CBDT in accordance with the scheme to be made by the Central Government.

Voluntary contribution received by an electoral trust would be treated as its income under section 2(24), but shall be exempt under section 13B if the trust distributes to a registered political party during the year, 95% of the aggregate donations received by it during the year along with surplus brought forward from any earlier years. Another condition for availing the benefit under this section is that the electoral trust should function in accordance with the rules framed by the Central Government.

It may be noted that the exemption under section 13B will be available only in respect of voluntary contribution received by an electoral trust. The exemption cannot be claimed in respect of any other income of the electoral trust.

Therefore, the given statement is not correct.
1. Where an institution engaged in imparting education incidentally makes profit, would it lead to an inference that it ceases to exist solely for educational purposes?

Queen’s Educational Society v. CIT (2015) 372 ITR 699 (SC)

Facts of the case: The assessee, an educational institution, showed a net surplus of ₹ 6.59 lakhs and ₹ 7.83 lakhs, respectively, for the assessment years 2000-01 and 2001-02. Since it was established with the sole object of imparting education, it claimed exemption under section 10(23C)(iiiad). The Assessing Officer rejected the claim of exemption on the ground that the assessee has made profits and did not exist solely for educational purposes. The Commissioner (Appeals) allowed the assessee’s claim and the Tribunal dismissed the Revenue’s appeal holding that the assessee was engaged undoubtedly in imparting education and the profit was only incidental to the main object of spreading education. However, the High Court restored the order of the Assessing Officer on the reasoning that the institution made profit, year on year, and hence, was not eligible for tax exemption.

Supreme Court’s Observations: The Supreme Court observed that the provisions of section 10(23C)(iiiad) provide for three requirements, namely,

(i) the education institution must exist solely for educational purposes;
(ii) it should not be for purposes of profit; and
(iii) the aggregate annual receipts of such institution should not exceed the amount as may be prescribed. Such monetary limit is ₹ 1 crore as per Rule 2BC.

The Supreme Court concurred with the Tribunal’s reasoning that profit is only incidental to the main object of spreading education. If there is no surplus arising out of the difference between receipts and outgoings, the trust will not be able to achieve the objectives. Any education institution cannot be run in rented premises for all the times and without necessary equipment and without paying to the staff engaged in imparting education. The assessee is not getting any financial aid/assistance from the Government or other philanthropic agency and, therefore, to achieve the objective, it has to raise its own funds. However, such surplus would not come within the ambit of denying exemption under section 10(23C)(iiiad).

Further, the Apex Court made reference to the tests culled out in its own decisions in the case of Addl. CIT v. Surat Art Silk Cloth Manufacturers Association [1980] 121 ITR 1, Aditanar Educational Institution v. Addl. CIT [1997] 224 ITR 310 and American Hotel and Lodging Association Educational Institute v. CBDT [2008] 301 ITR 86, which would apply for determining whether an educational institution exists solely for education purposes and not for purposes of profit.
The Apex Court, after analyzing the legal provisions and precedents, summed up the law common to section 10(23C)(iiiad)/(vi):

(a) Where an educational institution carries on the activity of education primarily for educating persons, the fact that it makes a surplus does not lead to the conclusion that it ceases to exist solely for educational purposes and becomes an institution for the purpose of making profit;

(b) The predominant object test must be applied – the purpose of education should not be submerged by a profit making motive;

(c) A distinction must be drawn between the making of surplus and an institution being carried on “for profit”. Merely because imparting of education results in making a profit, it cannot be inferred that it becomes an activity for profit;

(d) If after meeting expenditure, surplus arises incidentally from the activity carried on by the educational institution, it will not cease to be one existing solely for educational purposes; and

(e) The ultimate test is whether on an overall view of the matter in the concerned assessment year, the object is to make profit as opposed to educating persons.

**Apex Court’s Decision**: Based on the above principles and tests, the Apex Court upheld the Tribunal’s view that the assessee was engaged in imparting education and the profit was only incidental to the main object of spreading education. Hence, it satisfies the conditions laid down in section 10(23C)(iiiad) for claim of exemption thereunder.

2. **Would imparting education/training in specialized field like communication, advertising etc. and awarding diplomas/certificates constitute an “educational purpose” for grant of exemption under section 10(23C)(vi)?**


**Facts of the case**: The assessee-society registered under the Societies Registration Act, 1860 as well as under the provisions of the Bombay Public Trust Act, 1950 was engaged in imparting higher and specialized education. It imparted education in the field of communication including advertising and its related subjects. It was granted registration under section 12A of the Act originally.

The assessee later submitted an application for exemption under section 10(23C)(vi) and for which after calling for details, the CIT refused to grant exemption under section 10(23C)(vi). The reasons for refusal were (i) the society was not having education as the sole purpose; (ii) it is engaged in conducting coaching / training courses for and on behalf of industry, trade and commercial organizations; (iii) it is engaged in various social activities of general public utility; and (iv) it was not conducting educational courses as charitable activity but for the purpose of making profit.
High Court’s view: The Court noted that the object clause of the society which indicated that the institution was awarding diplomas, certificates etc after providing training in communication, advertising and related subjects. The memorandum of the assessee showed that the fee collected shall not exceed the cost of training, hostel expenses etc and it is not precluded from subsidizing such costs. It observed that providing training to the individuals as well as those persons who have been sponsored by the companies to meet the needs of Indian industry and commerce, would not make the assessee-society as carrying on activity of service in relation to any trade, commerce and industry.

It held that teaching does not mean teaching the students only in the manner and method, the regular schools or colleges adopt to teach. In the progressive world, it is expected from certain institutions that they educate, teach and train persons so that those persons can compete with similar experts worldwide. It thus rejected the argument of the Revenue and held that providing latest information and training to persons to become super specialists in a particular field would still be treated as education.

Supreme Court’s Observations: The Apex Court took note of the observations of the High Court and made reference to its own precedent in the case of Queen’s Educational Society v. CIT (2015) 372 ITR 699 (SC) where it had summarized the legal position as under:

“The law common to sections 10(23C)(iiiad) and (vi) may be summed up as follows:

(i) Where an educational institution carries on the activity of education primarily for educating persons, the fact that it makes a surplus does not lead to the conclusion that it ceases to exist solely for educational purposes and becomes an institution for the purpose of making profit;

(ii) The predominant object test must be applied – the purpose of education should not be submerged by a profit making motive;

(iii) A distinction must be drawn between making of a surplus and the institution being carried on ‘for profit’. No inference arises that merely because imparting education results in making a profit, it becomes an activity for profit;

(iv) If after meeting the expenditure, a surplus arises incidentally from the activity carried on by the educational institution, it will not cease to be one existing solely for educational purposes;

(v) The ultimate test is whether on an overall view of the matter in the concerned assessment year, the object is to make profit as opposed to educating persons”.

The Apex Court, in Queen’s Educational Society’s case, noted the divergence of opinion among various High Courts on this issue. In that case, it had approved the decision of Delhi, Bombay and Punjab & Haryana High Courts and set aside the judgement of Uttarakhand High Court.
The Apex Court held that the correct tests for determining whether an institution exists solely for educational purposes and not for the purposes of profit were laid down in the Supreme Court decisions in CIT (Addl.) v. Surat Art Silk Mfg. Association (1980) 121 ITR 1; Aditanar Educational Institution v. Addl. CIT (1997) 224 ITR 310; and American Hotel & Lodging Assn. Educational Institute v. CBDT (2008) 301 ITR 86.

It further observed that the Thirteenth proviso to section 10(23C) is of great importance to the assessing authorities who must continuously monitor from assessment year to assessment year to know whether such institutions continues to apply their income and invest or deposit their funds in accordance with the law laid down. The activities of such institutions must be looked at carefully. If they are not genuine or are not being carried out in accordance with all or any of the conditions subject to which approval was given earlier, such approval and exemption must forthwith be withdrawn.

**Supreme Court’s Decision:** Applying the rationale of the Supreme Court ruling in Queen’s Educational Society’s case, the Apex Court, in this case, held that the institution is established for the sole purpose of imparting education in a specialized field. The Supreme Court, thus, allowed the petition and set aside the order of the Chief Commissioner of Income-tax refusing exemption under section 10(23C)(vi).

**Note:** Institutions engaged in providing specialized training in certain fields and awarding diplomas and certificates are also eligible for tax exemption in terms of section 10(23C)(vi). It is not mandatory for such institutions to impart education in formalized manner or conduct only recognized educational courses. Further, when corporates depute employees for gaining specialized knowledge, such imparting of knowledge by the institution would not mean that the institution is engaged in the activity of general public. Making of profit incidentally will not make the institution as existing for making profit. This is the jist of the above Supreme Court ruling.

3. In a case where the charitable trust is deemed to be registered under section 12A due to non-disposal of application within the period of 6 months, as stipulated under section 12AA(2), from when would such deemed registration take effect?


**Facts of the case:** In the present case, the Allahabad High Court held that once an application for registration of the trust is made under section 12A and in case the same is not responded to within six months, the trust would be deemed to be registered under section 12AA. The High Court opined that non-consideration of the application for registration within the time fixed by the legal provision would lead to deemed grant of registration and there is no reason to make the assessee suffer merely because the Income Tax Department is not able to keep its officers under check and control so as to take timely decisions on the matter.
The Revenue appealed against this decision and raised an apprehension that since the
date of application was February 24, 2003, the deemed registration would operate only after
six months from the date of application.

Supreme Court’s Decision: The Apex Court clarified that deemed registration would
commence only after 6 months from the date of application. Therefore, the registration of
the application under section 12AA of the Income-tax Act, in the case of the assessee trust
shall take effect from August 24, 2003.

Note:
This decision is based on the provisions of section 12A prior to insertion of clause (aa) in
sub-section (1) of section 12A and sub-section (2) in section 12A by the Finance Act, 2007
with effect from 1st June, 2007. The position prior to the amendment by the Finance Act,
2007 was that an application for registration has to be made before the expiry of one year
from the date of creation of the trust. However, where an application for registration was
made thereafter, the exemption provisions under sections 11 and 12 would apply from the
date of creation of the trust, if the Principal Commissioner or Commissioner, for reasons to
be recorded in writing, is satisfied that the person in receipt of the income was prevented
from making the application before the expiry of one year. If he is not so satisfied, the
exemption would apply from 1st day of the financial year in which the application was made.
The Finance Act, 2007 has inserted sub-section (2) in section 12A to provide that where an
application has been made on or after 01.06.2007, the provisions of section 11 and 12 shall
apply in relation to the income of such trust from the assessment year immediately following
the financial year in which such application is made.

In Society for the Promotion of Education’s case, the Supreme Court has decided that the
deeded registration would be effective only after six months from the date of application, in the
sense, that it would not have retrospective application. The Supreme Court ruling assumes
significance in the current context, since it affirms that non-consideration of application within
the time period of six months from the end of the month in which application is received would
tantamount to deemed registration. However, in the light of the current provisions of section
12A(2), the exemption provisions of sections 11 and 12 would apply in relation to the income of
the trust from the assessment year immediately following the financial year in which such
application is made, even though the effective date of deemed registration would be after expiry
of the six month period as per the above Supreme Court ruling.

4. Where a charitable trust applied for issuance of registration under section 12A within
a short time span (nine months, in this case) after its formation, can registration be
denied by the concerned authority on the ground that no charitable activity has been
commenced by the trust?

DIT (Exemptions) v. Meenakshi Amma Endowment Trust (2013) 354 ITR 219 (Kar.)

Facts of the case: In the present case, the assessee, being a trust, made an application
under section 12A for issuance of registration within nine months of its formation. The
registration authority issued a show cause notice to the assessee-trust to furnish its audited accounts as also material indicating the actual activities undertaken by the trust. In response to the said notice, the assessee-trust furnished the details, wherein it indicated that it has not yet commenced any charitable activity. The concerned registration authority, not being satisfied with the reply, refused to grant registration to the trust on the ground that it has not commenced any charitable activity.

**Issue:** The issue under consideration is whether registration under section 12AA can be denied on the ground of non-commencement of charitable activity, where an application for registration has been made within a short-time span after the formation of the trust.

**High Court's Observations:** On this issue, the Karnataka High Court opined that an application under section 12A for registration of the trust can be sought even within a week of its formation. The activities carried on by the trust are to be seen in case the registration is sought much later after formation of the trust.

The High Court further observed that, in this case, the corpus fund included contribution made by the trustees only, which indicated that the trustees were contributing the funds by themselves in a humble way and were intending to commence charitable activities. Also, it was not the Revenue’s contention that the assessee-trust had collected lots of donations for the activities of the trust, by the time its application came up for consideration before them. When the application for registration was made, the trust, therefore, did not have sufficient funds for commencement of its activities.

**High Court's Decision:** The High Court observed that, with the money available with the trust, it cannot be expected to carry out activity of charity immediately. Consequently, in such a case, it cannot be concluded that the trust has not intended to do any activity of charity. In such a situation, the objects of the trust as mentioned in the trust deed have to be taken into consideration by the authorities for satisfying themselves about the genuineness of the trust and not the activities carried on by it. Later on, if it is found from the subsequent returns filed by the trust, that it is not carrying on any charitable activity, it would be open to the concerned authorities to withdraw the registration granted or cancel the registration as per the provisions of section 12AA(3).

5. In a case where properties bequeathed to a trust could not be transferred to it due to ongoing court litigation and pendency of probate proceedings, can violation of the provisions of section 11(5) be attracted?

*DIT (Exemption) v. Khetri Trust (2014) 367 ITR 723 (Del)*

**Facts of the case:** As per the ‘will’ of Late Raja Bahadur Sardar Singh, the entire property, including immovable property and shares in foreign companies, were bequeathed to the trust. However, the properties could not be transferred to or acquired by the trust because of ongoing litigation in the Court. In the probate proceedings, the ‘will’ was challenged and the probate proceedings are still pending.
The trustees paid ₹ 1,10,000 for raising a memorial for late Raja Bahadur Sardar Singh and the said amount was given to a business entity for this purpose, but due to the ongoing dispute, such project was not completed. The business entity, however, paid interest on the said amount. The Assessing Officer denied the benefit of exemption under section 11, on the ground that the asset held in the form of shares of foreign company and the advance given to business entity were contrary to the mandate of section 11(5) and thus, the condition specified in section 13(1)(d) has been violated.

**Appellate Authorities’ views:** The Commissioner (Appeals) observed that the validity of the will has been challenged in the probate proceedings; therefore, till the ‘will’ is probated and affirmed as genuine, the trust would not acquire the legal right on the property for the purpose of Income-tax Act, 1961. In case the probate is denied, the properties would not devolve on the trust. The shares in foreign company were still in the name of the donor, Late Raja Bahadur Sardar Singh, and its acquisition by the trust is dependent upon the adjudication of the probate.

Further, with regard to the advance given to the business entity, the Commissioner (Appeals) found that the said amount cannot be treated as an investment which was covered and regulated by section 11(5), since the intent and purpose behind the payment was not investment.

These views of the Commissioner (Appeals) were confirmed by the Tribunal.

**High Court’s Decision:** Based on the above factual findings, elucidated and affirmed by the Commissioner (Appeals) and the Tribunal, the High Court held that there was no violation of section 11(5) in this case.

6. **Is the cancellation of registration of a trust under section 12AA, on the basis of search conducted in the premises of its Secretary General and the statement recorded by him under section 132(4), valid?**

**U.P. Distillers Association (UPDA) v. CIT [2017] 399 ITR 143 (Del)**

**Facts of the case:** A search and seizure operation took place in the premises of the Secretary General of the assessee, that is, Uttar Pradesh Distillers Association, in February 2006. During the search, the Secretary General’s statement was recorded under section 132(4) of the Act. The statement was retracted after two years. In the meanwhile, the Commissioner of Income-tax (CIT) cancelled the assessee’s registration under section 12AA(3) on the basis of the search operation and the statement made. The order was upheld by the Appellate Tribunal. The assessee contended that Secretary General’s statement was made in the course of search in respect of his premises and not those of the assessee. Hence, the Secretary General’s statement was not attributable to the assessee nor could the materials indicated by him be the basis for cancellation of registration of the trust under section 12AA.
**Issue:** The issue under consideration is whether the cancellation of registration under section 12AA as a charitable trust on the basis of search conducted in the premises of the Secretary General of the assessee-trust and the statement recorded by him under section 132(4) is valid.

**Delhi High Court’s Observations:** The Court dismissed the appeal to hold that although the premises, in which the search under section 132 took place, belonged to the Secretary General, he virtually ran the assessee-trust’s activities from the same premises. The information which he provided in the course of the search pointed out to the activities of the assessee-trust and not to his own activities. Further, the Tribunal had expressly recorded that the search proceedings took place in the context of section 153A, in the very premises of the Secretary General, with respect to the assessee-trust.

**Delhi High Court’s Decision:** The Delhi High Court, accordingly, held that cancellation of the trust’s registration under section 12AA on the basis of search conducted in the premises of the Secretary General and the statement recorded under section 132(4) from him, is valid.

**Note:** The special leave petition filed against the aforementioned decision of the Delhi High Court was dismissed by the Supreme Court.

7. Is the approval of Civil Court mandatory for amendment of trust deed, even in a case where the settler has given power to the trustees to alter the trust deed?

**DIT (Exemptions) v. Ramoji Foundation (2014) 364 ITR 85 (AP)**

**Facts of the case:** The settler gave power to the trustees to amend, alter, change or modify the objects of the trust deed with the approval of two-third majority. Such additional or altered object, however, must be of charitable nature falling within the definition thereof under the relevant provisions of the Income-tax Act, 1961. Based on these provisions of the trust deed and referring to the Supreme Court decision in *CIT v. Kamla Town Trust (1996) 217 ITR 699*, the Tribunal held that the trust deed can be amended without approaching the Civil Court. Therefore, the Tribunal directed the DIT (Exemptions) to grant registration to the assessee-trust under section 12AA on the basis of the amended trust deed.

**Issue:** The issue under consideration before the High Court is whether the Tribunal was correct in holding that the amendment to the trust deed can be made without approaching the Civil Court, on the basis of the decision in the case of *Kamla Town Trust (Supra)*.

**High Court’s Observations:** The High Court observed that the power has been given to the trustees by the settler to amend the trust deed without approaching the Civil Court, provided all the conditions laid down by the settler are fulfilled. The sanction of Civil Court is required only when there is no such power. When the power has been specifically given to the trustees by the settler, no further power from the Civil Court is required.
The High Court made reference to the Kamla Town Trust’s case and observed that it has not been stated anywhere in the Supreme Court’s decision that in spite of the power given to them by settler to amend the trust deed, the trustees have to approach the Civil Court to get the trust deed rectified.

**High Court’s Decision:** Accordingly, in this case, the High Court held that the Tribunal has correctly dealt with the matter and the trust deed amended by the trustees can be relied upon by the Revenue authorities for the purpose of granting registration under section 12AA.