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Charitable Contributions: The Indian Tax System & Recommendations

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1. Introduction

In the earlier chapters we have already explored the relevance of Non-Governmental Organizations whether public Trusts, associations, or other non-profit entities (including non-profit companies) and how they perform a vital role in supplementing governmental efforts in promoting economic development and social welfare.

Tax administrations world over recognize voluntary effort and provide incentives to genuine charitable organizations. Most often, this is done by either partially or fully exempting their incomes from tax, and also by providing tax incentives to donors in order to encourage them to contribute resources to such organizations.

Secular social objectives such as promotion of education, medical care and other kinds of charity are some areas in which efforts of the State are always inadequate, given the size of our country and the large section of the population that needs such care and protection. Therefore, the State has always recognized and sought to encourage the laudable role of private philanthropy in relieving distress and in helping to meet the socio-economic, cultural, medical, educational and religious needs of the society. To encourage the contributions of such Private Philanthropy (Charitable Trusts/Institutions) in catering to the needs of the society, tax concessions have been granted to them under the Indian Taxation system. Sections 2(15), 2(24)(iia), 10 (23C), 11, 12, 12AA, 13, 80G, 115BBC and 139 (4C) of the Income-Tax Act 1961 deal with exemptions available to income of Trusts and institutions created for charitable or religious purposes, subject to fulfillment of certain conditions. Since the tax concessions afforded to these institutions involve a sacrifice of public money, it became imperative to ensure that tax privileges are not abused and they are enjoyed only by those charitable and religious institutions which actually deserve them.

There has been rapid growth of Non-Governmental Organizations and institutions in recent years in the areas of education, social and medical sectors which are getting registered for claiming exemptions from taxation on their income derived from their charitable and religious activities under the provisions of Act. Many private schools, colleges, coaching centers, hospitals, local authorities etc. are running as charitable Trusts/institutions to avail tax exemptions. A number of questions on the charitable character of these organizations and institutions have been raised from time to time and only 3 percent of the assessees (51,570 Trusts) claimed 96 per cent (7,602,283 cr) of total deductions/exemptions.

2. The Legal and Fiscal Framework

"Charity is on the concurrent list of subjects where both the Center and the States are competent to legislate. Accordingly, some of the laws are Central and applicable all over India, while others are enacted by individual states. There are five main laws governing the non-profit sector, each of which is administered by an agency specifically created for the purpose. These are:

- The Registration of Societies Act of 1860, a Central Act, and its versions enacted by different states, with a Registrar of Societies in each state to register and regulate organizations registered under this Act.

- There is no Central Act for registering or regulating public charitable Trusts. A variation of the Indian Trusts Act of 1882, which applies only to private Trusts, is in force in different states. Maharashtra and Gujarat have offices of the Charities Commissioner, created under the Bombay Public Trusts Act, 1950, to oversee charities in these states; Tamil Nadu has a Department of Religious and Charitable Endowments, and other states have some similar organization for charitable Trusts.

- Section 8 of the Companies Act 2013, deals with nonprofit companies. It is administered by the Registrar of Companies.

- The Income Tax Act, 1961, (IT Act) again a Central Act applicable all over India, provides fiscal benefits to NPOs, the administrative agency being the Department of Income Tax Exemption, and

- The Foreign Contributions Regulation Act, (FCRA) a Central Act applicable all over India, was essentially a security measure to control external funds flowing to nonprofit organizations, which could be used to threaten national security. In practice it has come to regulate the receipt and spending of all foreign funds going to nonprofit organizations, irrespective of security concerns."[1]

3. Legal provisions

The legal provisions under which registration/approval are granted to the Charitable Trusts and Institutions (Trusts) are section 12A by CIT and section 10(23C) by DGIT of the IT Act. Other relevant provisions dealing with application of money received by such institutions, issuance of

[1]A Review of Charities Administration in India - Sampradaan Indian Centre for Philanthropy (Sponsored by the Planning Commission, Govt. of India – September 2004)

notifications for sanctions and allowance of exemption from taxation including filing of returns under Act are available in Sections 2(15), 2(24)(iia), 10(23C), 11, 12, 12AA, 13, 80G, 115BBC, 139(4A) and 139(4C) of the IT Act. Besides, there are certain circulars and instructions issued by CBDT and judicial decisions regarding registration/approval and assessment of Trusts. The Trust should, therefore, be one established in accordance with law and its objects should fall within the definition of the term "Charitable purpose".

4. Charity Vs Philanthropy

The terms Charity and Philanthropy are often used interchangeably but there is a significant difference. Charity is an empathetic response to a crisis or catastrophe. Charity tends to be a short-term, emotional, immediate response, focused primarily on rescue and relief, whereas philanthropy is much more long-term, more strategic, focused on rebuilding. There is charity, which is good, and then there is problem-solving charity, which is called philanthropy, Philanthropy, then, is the preferred method because it not only seeks to help, but intentionally searches for the root of the problem and looks for solutions.

5. Charitable Purpose – Section 2(15) of the IT Act

The term "Charitable purpose" as laid down under section 2(15) has undergone a series of change over financial years by array of amendments. While limbs of charitable purposes from (i) to (v) have been fairly unchanged, understanding and interpretation of terms like 'Relief of poor' and others have always been the matter of litigation.

Sec. 2(15) defines charitable purpose as including –

i) relief of the poor;
ii) education;
iii) medical relief;
iv) preservation of environment (including water sheds, forests and wild life);
v) preservation of monuments or places or objects of artistic or historic interest and
vi) the advancement of any other object of general public utility.

The above definition was substituted by the Finance Act, 2008 with effect from 1-4-2009. To understand the exact position arising from amendment in Section 2(15) in 2008 effective from Assessment Year 2009-10, it is necessary to know the background of the amendment as stated by the Finance Minister while moving the amendment.

The Finance Minister had amended the definition of charitable purpose given in Section 2(15) by the Finance Act, 2008 with effect from 1-4.2009 by adding a proviso to the Section of just five lines. In para 180 of the Budget speech, the Finance Minister stated as follows:

> *"Charitable purpose" includes relief of the poor, education, medical relief, and any other object of general public utility. These activities are tax exempt, as they should be. However, some entities carrying on regular trade, commerce or business or providing services in relation to any trade, commerce or business and earning incomes have sought to claim that their purpose would also fall under "charitable purpose". Obviously, this was not the intention of Parliament and, hence, I propose to amend the law to exclude the aforesaid cases. Genuine charitable organisations will not in any way be affected."*(emphasis supplied)

It is thus pertinent to note that the intention of Finance Minister was only to exclude from exemption entities carrying on business and earning income for which exemption was claimed on the basis that the purpose would fall under charitable purpose. The actual effect of the amendment is however far reaching and going much beyond the case of the above entities.

> *"Provided 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."*

One of the land mark development was laid in Finance act 2008, whereby if the main purpose of the Trust is advancement of any object of general public utility, and also it carries out any trade or commerce or business for any consideration irrespective of the way or nature by which such considerations or fees are applied. This created a lot of ambiguity on applicability of this provision towards other limbs and circular 11 of 2008 dated 18-Nov-2008 was issued whereby it was clarified that restriction on carrying on trade or commerce or business is not in respect of relief of the poor, education, or medical relief.

This gave a major relief to Trust claiming exemptions under Section 10(23C) or Section 11(4) and satisfying the conditions stipulated under respect sections with prime objects of relief to poor or education or medical relief by making their activity's to be treated as charitable purpose even if they incidentally carry on a commercial activities.

This provision however impacted significantly smaller Trusts, which were incidentally undertaking minor trade activities. In order to give relief to them, Government issued a second proviso to section 2(15) vide the Finance Act 2010 with retrospective effect from 1.4.2009, which

read as under "The first proviso shall not apply if the aggregate value of the receipts from the activities referred to therein is Rs 10 lakh or less in previous year."

This ensured that if receipts from trade activity are less than or equal to Rs 10 lakhs then the same will be eligible to be classified as charitable purpose. This was a savior for smaller Trust who are completely dependent on voluntary contributions. The above limit of Rs 10 lakh has been subsequently increased to Rs 25 lakh with effect from 01.04.2012.

In the same Finance Act 2012, Section 13(8) has been inserted retrospectively from AY 2009-10 which provides that exemption under Section 11 or 12 shall not be allowed if limit specified under first proviso of Section 2(15) is exceeded i.e. if incidental trade activities carried on are more than Rs 25 Lakh.

Although the same provisions of Section 13(8) have been enacted, it will not impact the Trust from losing its registration but only will affect the exemption for the particular year.

The Income Tax Appellate Tribunal ("ITAT") Bench in **Ghatkopar Jolly Gymkhana vs. DIT(E)**[2] has set aside the order of DIT, cancelling assessee's registration as charitable Trust u/s 12A; Assessee not entitled to enjoy tax benefits as gross trade/ business receipts exceeded specified limit of Rs 10 lakhs as per second proviso to Sec. 2(15); Violation of the condition only impacts assessee's right to claim tax exemption for the relevant "previous year"; It does not impact Trust's registration or ability to claim exemption for future years; Trust can carry out business activities without losing identity, but gross receipts limit of Rs 10 lakhs should not exceed to avail tax exemptions; the ITAT has kept its Reliance on the co -ordinate bench ruling in **Rajasthan Housing Board vs. CIT**[3].

Yoga included in definition of Charitable purpose

The Term "Charitable Purpose" has been amended by Finance Act, 2015 to include Yoga as an activity of charitable nature. The Courts have taken a divergent stands while considering Yoga as a charitable activity but on the limb under which such categorization can be made, the Bombay High court in **CIT v. Rajneesh Foundation**[4]**,** held that the charitable Trusts/ organization whose main object is propagation and teaching of Yoga will be classified under objects of general public utility.

[2] (TS-546-ITAT-2013(Mum))
[3] [[2012] 51 SOT 383 (JP)]
[4] [2006] 280 ITR 553 (Bom.)

The ITAT Bench in Divya Yog Mandir Trust vs. JCIT[5] has taken the stand that Yoga can be safely accepted as a system fit into the definition of 'medical relief'; Rejecting the Revenue's stand that yoga unlike other medical systems not a curative system for alleviating diseases, but only a spiritual system; The Bench has kept its reliance on Clinical Establishment Act 2010, where yoga is recognized as a system of medicine under clause (h) of section 2.

The Supreme Court in the case of LokShikshana Trust had explained the meaning of the word 'education' in the context of Sec 2(15) of the IT Act. As per this decision, the education is the process of training and developing the knowledge, skill, mind and character of students by schooling by way of systematic instruction, schooling or training.

While the classification made by ITAT of Delhi and SC in LokShikshana Trust would be benefiting the Trust the classification under Bombay High Court judgment would negate the impact on the assesse as, if total consideration from such activity is more than Rs 25 Lakh then the Trust will not be eligible for exemption as the same will not for chartable purpose.

This amendment by introducing Yoga has one of the limbs of charitable purpose, has put an end to differential classification and facilitated the institutions registered under section 12AA/propagating, teaching by holding camps, classes etc. by making them eligible for exemption without fitting for the residual limb and thereby not restricting them to carry on any commercial activity or trade or commerce which is incidental to the objects of the Trust.

Amendment to Proviso to section 2(15) of the IT Act

The proviso under section 2(15) of the IT Act has been amended by which the limit of Rs 25 Lakh has been replaced with percentage of gross receipts being 20 %.

This implies that in place of consideration from trade or commerce of Rs.25 Lakhs, a proportional or comparative limit on the gross receipt has been provided to decide whether activities of the Trust are charitable purpose or not.

This amendment comes with qualms and benefits, bigger Trust whose objects are general public utility having incidental trade activity would be benefited if the total receipts from such trade activity is more than the Rs 25 Lakh but such receipts are lesser than 20 % of the total receipts of the Trust.

It is worthwhile to recall a discussion of the Supreme court in Court in **Additional Commissioner of Income-tax, Gujarat v/s. Surat Art Silk Cloth Manufacturers Association**[6]. In that case,

[5] (TS -459 –ITAT 2013(Del)
[6] 121 ITR 1

while considering the expression "Activity for Profit" for the purposes of Section 2(15) of the IT Act, the Supreme Court held that the test that must be applied is not "whether as a matter of fact an activity results in profit" but "whether the activity is carried on with the object of earning profit". In other words where the predominant object of the activity is charitable purposes and falls within the first three limbs of section 2(15) purposes and not to earn profit, whether it would lose its character, will have to be considered in the light of facts of each case.

6. Distinction between object and its advancement

If the following interpretation of the proviso to section 2(15) of the IT Act is accepted, the proviso will not apply to such a Trust/society, which will continue to be exempt under section 11 of the IT Act. There is a distinction between the "advancement of any other object of general public utility" and object itself involving activities of general public utility; e.g. an institution for the blind carries on activities through the inmates to provide training to handicapped but the advancement of the objects in such a case does not involve activities for profit as the object itself is to carry on commercial activities by the blind inmates. In such a case the proviso to section 2(15) does not apply. On the other hand if the object itself does not involve carrying on commercial activities but for advancing such objects of the Trust/society commercial activities are carried on, then alone the proviso to section 2(15) of the IT Act does apply.

The distinction was noted by the Supreme Court in the case of **Indian Chamber of Commerce**[7] as follows: *"Dr. Pal for the assessee submits that the proper interpretation of Section 2(15) of the Income-tax Act, 1961, would be that the object of general public utility must itself involve the carrying on of any activity for profit. That was the main thesis of his argument. He therefore submits that the objects, as described in the memorandum of the assessee, Indian Chamber of Commerce, as such do not ipso facto involve the carrying on of any activity for profit within the meaning of section 2(15) of the Income-tax Act, 1961. We are unable to accept the submission of Dr. Pal for the assessee. We shall state our reasons briefly. The expression "the advancement of any other object of general public utility not involving the carrying on of any activity for profit" plainly indicates that it is not the object of general public utility which would involve the carrying on of any activity for the profit but the "advancement" of that object. Otherwise, it will lead to a self-contradictory situation because the reason for including the object of general public utility as a charitable purpose was that it was not a charitable purpose with a blanket cover for any object of general public utility but with the severe limitation that the advancement of an object of general public `utility would not involve the carrying on of any activity for profit or else it would not be a charitable purpose within the meaning of section 2(15) of the Income-tax Act, 1961. That, in our view, is the true import, meaning and significance of this new definition with expression "the advancement of any other object of general public utility not involving the carrying on of any*

[7] page 152 of (1971) 81 ITR 147

activity for profit". In other words, the advancement of any other object of general public utility would be a charitable purpose provided that its advancement does not involve the carrying on of any activity for profit. The wisdom behind the limitation is plain. The expression "object of general public utility" is an expression of wide import and it was therefore, thought necessary by Parliament in the wisdom to impose certain restriction on the area of the object of general public utility and the area selected is that its advancement must not involve the carrying on of any activity for profit." (emphasis supplied)

Thus, the submission made by us in this behalf is also supported by the observation of the Supreme Court in the above judgment and the contention can be extended to section 2(15) proviso also, which requires the advancement of object of general public utility to attract the proviso but if the object itself is to carry on commercial activities, then the proviso to Section 2(15) does not apply.

The Supreme Court in the case of **Surat Art Silk**[8] made a distinction between the phrases 'object of general public utility" and "advancement of object of general public utility". It is clear on a plain natural construction of the language used by the Legislature that the ten crucial words "not involving the carrying on of any activity for profit" go with "object of general public utility" and not with "advancement". It is the object of general public utility which must not involve the carrying on of any activity for profit and nor its advancement or attainment. What is inhibited by them in last ten words is the linking of activity for profit with the object of general public utility and not it's linking with the accomplishment or carrying out of the object. It is not necessary that the accomplishment of the object or the means to carry out the object should not involve an activity for profit. That is not the mandate of the newly added words. What these words require is that the object should not involve in the carrying on of any activity for profit. The emphasis is on the object of general public utility and not on its accomplishment or attainment.

The decisions of the Kerala and Andhra Pradesh High Courts in **CIT vs. Cochin Chamber of Commerce & Industry**[9] **and State Road Transport Corporation vs. CIT**[10] respectively, in our opinion, lay down the correct interpretation of the last ten words in section 2, clause (15). The true meaning of these last ten words is that when the purpose of a Trust or institution is the advancement of an object of general public utility, it is that object of general public utility, and not its accomplishment or carrying out, which must not involve the carrying on of any activity for profit."

A plain reading of the proviso to section 2(15) of the IT Act would immediately make it evident that the legislature has addressed precisely this distinction made by the Supreme Court, by stipulating that the advancement of any 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

[8] 121 ITR 1
[9] (1973) 87 ITR 83
[10] (1975) 100 ITR 392

even though the business income is used for charitable purposes. Therefore, the decisions of various Courts rendered prior to the amendment w.e.f. 1-4-2009 would not be applicable to A. Y. 2009-10 onwards.

The Income Tax Department has interpreted proviso to Section 2(15) of the IT Act regarding commercial activities in their favour by considering all activities of various types of Trusts/ institutions as commercial activities, so as to hold that the Trust/ institution ceases to be for charitable purpose and therefore it taxes their entire income allowing establishment expenses but including the amounts applied on the object of the Trust. They have also not accepted the contention that even if the proviso applied to the sixth object of general public utility, the tax should be restricted to income for sixth object but the income for educational, medical and five objects should not be liable to tax.

Thus, in the case of trade association and chambers of commerce, which were the main categories of Trusts covered by the Circular, exemption is denied on the ground that they are carrying on commercial activities like issuing certificate of origin, arbitration fees, and fees from holding examinations relating to commercial courses, etc. Further, as held by the Supreme Court in the case of **Yogiraj Charitable Trust vs. CIT[11],** if one of the objects ceases to be charitable as per the amendment, even though other objects may be charitable, the exemption would not be available. In other words the Trust cannot be partly for charitable purpose and partly for non-charitable purpose, with the one exception in Section 11(1)(b) i.e. Trust created before 1-4-1962.

Regarding the claim for exemption under section 11(4A), on the basis of the principle that all provisions of the Act are to be read harmoniously, it is held that the proviso governs only the last category i.e. general public utility, when one reads both sections 2(15) and 11(4A) together, it is clear that after the amendment of section 2(15), section 11(4A) would be applicable to a Trust, which is engaged in activities falling under the first five objects only and therefore, there was no need for an amendment to Section 11(4A) of the IT Act.

7. Mutuality

- As regards the principle of mutuality, the entire receipts from members are not exempt in view of provision of section 28(iii) of the Act, which states that income derived by trade, professional or similar association from specific services performed for its members would be income chargeable to tax under the head profits & gains of business. Therefore, incomes on account of specific services are brought to tax. Thus, income from issue of certificate of origin, arbitration fees, fees for holding commercial diploma examination, etc. are taxed under S.28(iii). The Supreme Court in the case of **CIT vs. Calcutta Stock Exchange**

[11] (1976) 103 ITR 777

Association Ltd.[12] held that the words specific service meant conferring on members some tangible benefit which would not become available to them unless they paid the specific fees charged for such specific benefit. Thus, the major part of the income is taxed under section 28(iii) of the IT Act and only the balance income, subject to deduction of relevant expenses, would be exempt as mutual income.

Amendment in practice

- In the case of educational institutions narrow meaning given by Supreme Court in the case of **Sole Trustee, Loka Shiskshana** Trust[13] is that formal education by schools, colleges and universities; the income is taxed in respect of all other educational activities by holding such activities as of commercial nature. It may be noted that there are several cases after the Supreme Court decision which have given a wider meaning to the term education, including observations in one of the cases that the Supreme Court has given a very restricted meaning to the term education.
  i) Ecumenical Christian Centre vs. CIT[14];
  ii) Indo –American Society vs. ADIT(E)[15];
  iii) CIT vs. Sri Thyaga Brahma Gana Sabha (Regd.)[16];
  iv) Guajarat State Co-operative Union vs. CIT[17];
  v) Prajapati Brahma Kumari Ishwariya[18];
  vi) CIT vs. Sangit Kala Mandir Trust[19]

- In the case of one educational Trust which runs several colleges and Institutions, the Management Development Programmes held by the Trust with different companies for development of managements skills involving faculty of the Trust is considered to be commercial activity as per the proviso to Section 2(15) of the IT Act merely on account of largeness of the amount and the number of such programmes. The Tribunal has reversed the order of CIT(A) but the Department has appealed to the Hon'ble Bombay High Court. Likewise, in the same case, the rental received from the hall and college properties is held to be business income and though, the Tribunal has reversed the Order of CIT(A) following Supreme Court judgment in Andhra Chamber of Commerce[20] and reaffirmed in (1981) 130 ITR 181 (SC), the Department has filed appeal to the Hon'ble Bombay High Court.

[12] 36 ITR 222
[13] (1975) 101 ITR 234
[14] (1983) 139 ITR 226
[15] (2005) 278 ITR (AT) 49
[16] (1991) 188 ITR 160 and 164 to 166
[17] 195 ITR 279
[18] 71 ITD 169 (Jaipur Tribunal)
[19] (1987) 166 ITR 217 (Cal.)
[20] (1965) 55 ITR 722 (SC)

- In case of a leading hospital Trust, the sale of medicines by the Pharmacy attached to the hospital is considered to be business income under 2(15) proviso on account of large amount of receipts.

- In case of sports clubs and gymkhanas, on account of sales of restaurant and rental from the property apart from game fees from members, the proviso to Section 2(15) is invoked to deny exemption under section 11 of the IT Act.

- In case of Trusts/societies for the Church operated by a Society, the receipts from sale of publications to improve the life and principles of good living are considered to be commercial activities for taxing the income of the Church.

- In case of large Panjrapole Trust, the sale of milk after distributing free maximum amount to poor persons and selling at subsidised price to hospital, old age homes, etc. the sale of milk to the public is considered to be commercial activity on the basis of the large amount and percentage to total sale for taxing the income.

- The above illustrations show that all Trusts for the general public utility will be considered to have ceased for charitable purpose under S.2(15) proviso. Even if part of the income is claimed exempt as mutual as per Board Circular, the same is substantially denied by invoking Section 28(iii) of the IT Act for receipts for specific services. The approach arises from the belief of the Government that most of the Trusts are not really charitable and don't deserve any exemption.

- One can think of a remedy in such cases to form a separate entity which may be a Trust taking over the activities of the existing charitable Trusts, which are considered as commercial activities under section 2(15) proviso. The new entity will pay the tax on its income after deduction of expenses, but the interest and other investment income of the charitable Trusts will not be liable to tax. Common trustees between the charitable Trust and the new Trust should be avoided so that it is not caught within the vortex of Section 13(2) and Section 13(3) of the IT Act. Of course, this is easier said than done depending upon the facts of each case and very careful attention will have to be given to the formation of the new Trust or entity.

- The last question affecting Section 2(15) proviso is whether purely religious Trusts are attracting the proviso. As reference to religious Trust is totally absent in Section 2(15), it can be contended that such Trusts should not be liable to tax under the amendment, as wherever religious Trusts were intended to be covered, there is specific provision in the IT Act like Section 13(1)(a), Section 115BC regarding anonymous donations, etc.

- The Income Tax department has in May 2013 issued a booklet on "Assessment of Charitable Trusts and Institutions (TPI Series 37)" wherein the only comment given on this is most vexed controversy in Para 3.2 is as follows: *"Prior to assessment year 2009-10, business income of a charitable Trust or institution was also eligible for exemption subject to conditions that such business should be incidental to the attainment of its objects and that separate books of account are maintained for such business. With effect from 1-4-2009 (i.e., from Asst. year 2009-10 onwards) however, the "advancement of any other object of general public utility" shall not qualify as a "charitable purpose" if the same involves the carrying on of any activity in the nature of trade, commerce or business, or rendering of any service in relation to any trade, commerce or business, for a consideration. This new restriction applies irrespective of the nature of use or application of the income arising from such activity. However, the rigour of this amendment has been reduced somewhat by a subsequent amendment brought in by the Finance Act, 2010 (with retrospective effect from 1-4-2009) to the effect that the said restriction shall not apply if the aggregate value of receipts from such activity during the given financial year does not exceed Rs 10 lakhs (Rs 25 lakhs from 1-4-2012)."* Thus, the booklet of the Department does not clarify at all when the advancement involves the carrying on of commercial activity. One expected that when a guidance is issued on the subject of charitable Trusts, it should have clarified beyond doubt the scope of amendment.

- To sum up, the assurance contained in the Finance Minister's speech that the genuine charitable organisations will not in any way be affected and caution in para 3.2 of CBDT circular that assessees who claim that their object is charitable purpose would be well advised to eschew any activity which is in the nature of trade, commerce or business, really reflect the approach of the Government to charitable Trusts.

8. Registration u/s.12A/12AA

<u>Processing the applications for registration</u>

It is a mandatory requirement for Charitable Trusts to get registration under the Act for claiming exemption. A Trust shall apply in the prescribed form along with necessary documents to CsCIT/ CsIT/ DsIT-E to get itself registered/ approved/ notified. Thereafter, the concerned authority after verifying the genuineness and objectives of Trusts shall issue or reject registration/ approval/ notification within the prescribed time limit of 6 months/ 12 months.

All public Trusts must be registered with the Commissioner of Income-tax under section 12AA of the IT Act by making an application in form No.10A before 1st July 1973 or within one year from the date of creation of Trust. The Section provided till 31st May, 2007 that where the

Commissioner was satisfied that there was sufficient cause for delay, the registration would be retrospective from the date of creation of the Trust, while other belated applicants would be granted registration from the first day of the financial year in which the application is made. With effect from 1st June, 2007 there is no provision for condonation of delay by the Commissioner and exemption shall be granted only from the financial year in which the application is made. Recently the trend in the subject is that the registrations are denied on several grounds which are not justified, giving an impression that the intention is to tax the charitable Trust right from the inception

The most common ground for rejection of the registration is that the Trust has not carried out any activities before applying for registration. The Allahabad High Court has held in the case of **Fifth Generation Education Society vs. CIT**[21], that at the time of application for registration, the Commissioner is not required to verify the application of income on objects of the Trust. He has to verify only whether the application is made in accordance with Section 12A and Rule 17A and whether Form 10A is properly filled up. He has to also verify whether the objects as per the Trust deed are charitable or not.

The Kerala High Court held in the case of **Self Employers' Service Society vs. CIT**[22] held that since the society has not done any charitable work and activities which it carried on were only for the purpose generating income for its members, the rejection of application of the Trust for registration under section 12AA was justified. Mercifully, an opportunity was given to the Society to file a fresh application when it started charitable work and the Commissioner was directed to consider such application. However, this case was decided on its peculiar facts.

It was held by the Delhi Bench of the Tribunal in **Aryan Education Society vs. CIT**[23] that after the insertion of Section 12AA w.e.f. 1-4-1997 the Commissioner is empowered to enquire about activity carried on by the Trust before passing the Order. The scope of the enquiry by the Commissioner is not limited to ascertaining whether objects of the Trust are charitable or not (Fifth Generation Education Society vs. CIT[24] distinguished.)

The Karnataka High Court in the case of **Sanjevamma Hanumanthe Gowda Charitable Trust vs. DIT(E)**[25] decided that for the purposes of registration under section 12AA, what the authorities have to satisfy about the genuineness of the activity of the Trust and how the income derived from the Trust property is applied to charitable or religious purpose and not the nature of the activity by which, the income is derived by the Trust. The Orders passed by the DIT(E) and the Tribunal were

[21] (1990) 185 ITR 634
[22] 247 ITR 18 (Ker.)
[23] 281 ITR 72 (Del)
[24] (1990) 185 ITR 634 (All)
[25] 223 CTR 533

set aside and the matter was remanded back to the Director for fresh consideration in accordance with law.

As the Trust is entitled and required to apply for registration immediately on the settlement of the Trust, the registration 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. Therefore, it is not necessary that the Trust should have commenced charitable activities at the time of application. All that Section 12AA requires is that the Commissioner shall call for such documents or information from the Trust as he thinks necessary in order to satisfy himself about (i) the genuineness of activities of the Trust (if commenced) and (ii) the objects of the Trust and make such enquiries, as he may deem necessary for satisfying himself for the two conditions and he shall either register the Trust by passing an Order in writing or if not satisfied pass an Order in writing refusing registration of the Trust, after giving reasonable opportunity to the Trust of being heard.

In spite of such clear position in law the DIT(E) goes beyond the limits specified above and asks for accounts of the Trust and questions the nature of the activity by which the income is derived.

9. Non-inclusion of Dissolution Clause in the Trust Deed

The second most common objection raised by the DIT(E) is whether Trust Deed contains a clause for dissolution of the Trust and in the absence thereof summarily reject the application for registration. A dissolution clause is viewed as necessary in case of dissolution of a Trust, its net assets after meeting all its liabilities, should not revert to its founder, members, directors, donors etc. but used for its objects. In the absence of dissolution clause, the corpus of Trust is susceptible to misuse at the time of dissolution.

However this stand of the DIT(E) is incorrect as a Trust is a perpetual entity and it need not have such a clause on dissolution. If in such a case a Trust wants to dissolve itself, if there is a proviso to hand over the income and property of the Trust to another Trust having similar objects, it can do so and the Charity Commissioner also cannot object to the same (In practice he does object, but the remedy may be to leave a small amount with the Trust) Therefore, it is not necessary to have a dissolution clause for the validity of the Trust Deed and yet the applications are wrongfully rejected by the DIT(E). If the clause for dissolution is there, then the Trust can be dissolved only as per the provision in the clause which normally provides that the Trust may be dissolved by the Trustees handing over the entire income and property of the Trust to another Trust with similar objects.

In the absence of any specific provision in IT Act with respect to dissolution clause, rejection of application for registration on this account is neither enforceable nor legally sustainable

Further the judicial decisions too are not in favour of the Department on this issue. Some of these cases are as under:

- Tara Educational and Charitable Trust vs DIT[26]
- Shree Prantij Dash ShrimaliVanikGyanti Trust vs. DIT[27] In this case, the Hon'ble ITAT has relied on the case of Shree Chargam Dash PorwadMahamandal vs. DIT.

The DIT(E) also considers whether the Trust carries on activities of commercial nature for the object of general public utility and refuses registration. As already discussed above, the DIT(E) has only to consider whether the objects of the Trust are charitable and whether activities are genuine. The application of Section 2(15) proviso has to be considered in the course of assessment and not at the time of registration under section 12A of the IT Act.

Another curious reason for rejecting the application when all reasons are exhausted is to consider that if the Trust has large surplus income from the activities carried on by it, the surplus itself is a sign of non-genuine activities. There is a difference between the genuineness of the activities and a Trust having surplus income from activities, which may still be genuine. Therefore, to reject the application on the ground of surplus implying non-genuine activities is absolutely incorrect.

Another difficulty in the registration of the Trust is that the application is accepted only after the Trust has applied for registration under Bombay Public Trust Act. The registration under B.P.T. Act can take a long time, say more than six months, before registration is granted. Sometimes, there may be a delay on account of the fact that the Charity Commissioner considers whether a Trust is charitable under B.P.T. Act or not. If a Trust is constituted under Deed of Trust showing settlement of property for a charitable purpose, the DIT(E) can decide whether the Trust is for charitable purpose without waiting for registration under the B.P.T. Act. Moreover, statute similar to B.P.T. Act is not applicable in all the States of India and therefore, the registration u/s.12A cannot be linked up to the registration under B.P.T. Act. Hence, instructions should be issued to accept application for registration without insisting on the application for registration under B.P.T. Act.

10. Sec.12A in practice

We may consider some of the actual cases where the applications were rejected by the DIT(E). In the case of a Foundation for Research by the Trust, the application was rejected because research was not actually commenced. In the case of sports, Clubs and Gymkhanas already in existence,

[26] (ITA no 1247/Mum/2013 dated July 18, 2014)
[27] (ITA no 407/Ahd/2013 dated June 21, 2013)

the applications were rejected on the ground that they were carrying on commercial activities like – restaurant and charging fees for the games resulting in large surplus. As stated above, 2(15) proviso cannot be considered at the time of registration but only in the course of assessment. In case of a Welfare Fund set up by a Stock Exchange as per requirement of SEBI, the application was rejected on the ground that a fund to reimburse persons suffering loss on account of default by the Stock Exchange members or investors was not a charitable purpose but a fund for reimbursement of commercial losses. It was overlooked that any member of the public, rich or poor, was entitled to be reimbursed the loss and the Stock Exchange itself was a different entity from the Welfare Fund which compensated the member of the public for the loss suffered by him and even if such member of the public was not a poor person, it does not cease to be charitable. Eleemosynary element is not essential for a charitable Trust, which can be both for poor and rich persons but which cannot be restricted only to rich persons.

In the case of a Trust owning and maintaining a sanatorium for the convalescent persons the application was rejected on the ground that the sanatorium was being given to persons who were not treated by the Trust medically, thereby holding that it was a guest house other than sanatorium, though, the application clearly stated that the applicants were requiring the sanatorium for convalescence.

In the case of a Trust for the improvement of the City by providing plans for gardens, jogging park and other beautification projects, registration was refused on the ground that the objects of the Trust were not for general public utility, though, the documentary evidence was produced for the projects carried out in the metropolitan City of Mumbai.

In the case of an association of building contractors for the promotion of the interest of the builders in the building trade, the registration was refused on the ground that the appellant carried on non-genuine activities within the meaning of Section 12AA(3) of the IT Act and cancelled the registration retrospectively with effect from A. Y. 2009-10. The Bombay High Court has however held in the case of **Sinhagad Technical Education Society vs CIT**[28] that the DIT(E) can cancel the registration with retrospective effect.

Finally, the provision of Section 12AA(3) should be noted that once the registration is granted, it can be cancelled only if the registration was granted even though the objects were not charitable or the activities of the Trust were not genuine. Of course, registration under section 12AA does not mean that the Trust is automatically entitled to the exemption under section 11 of the IT Act each year. However, such registration is certainly an evidence of the fact that the objects of the Trust were charitable or religious in nature. An Assessing Officer cannot deny exemption under

[28] 343 ITR 23

section 11 to a Trust registered under section 12AA on the ground that its objects are not charitable in nature, as held in **Stock Exchange, Ahmedabad vs. ACIT**[29].

The Madhya Pradesh High Court held in **Madhya Pradesh Madhyam vs. CIT**[30] that the proceedings for registration are different from assessment proceedings and registration is binding on Income Tax authorities.

Section 12AA/ Rule 11AA(6) of the IT Rules provides that Commissioner shall pass an order for registration/ notification under section 12A/ 80(G) or reject the application within six months from the date on which such application was made. However, Section 10(23C) provides time limit for granting approval or rejecting the application within a period of 12 months from the end of the month in which such application is received.

Act is not explicit about the consequences/ remedies available in case an application is not processed within six months. Though there is a provision for appeal against refusal, no provision is there with regard to the delay made in processing the application. However, it was held that the purpose of providing six months' time limit to the CIT would become meaningless if there is no cause of action or outcome at the end of six months. Therefore, after the expiry of six months the registration will be deemed to have been granted.

As regards the action initiated to ensure that time limit for passing order under section 10(23C), 12A and 80G of the Act is adhered invariably in all the cases, the Ministry stated as under:

Further, proposal to make time barring limit uniform in respect of sec. 12AA & 80G applications by allowing extended time for completion in respect of section 12AA applications by excluding time taken by applicants to comply with Commissioner's directions as available presently under section 80G is under examination. This would also give applicants extended time for compliance and avoid rejections on account of compliance delays on their part. The suggestion is being examined in CBDT.

The plan to introduce web based interactive platform for applying for registration, submitting soft copy of necessary documents and communicating with each other, as far as practicable thus making the whole process faster, smoother, transparent and less time consuming. The Ministry replied that the feasibility of such type of web based interactive plan is under discussion.

To sum up the approach of the IT Department seems to be to deny registration at the 'fall of the hat' as illustrated by a few cases cited above and the policy seems to be to deny registration more than to grant the same so as to tax the charitable Trust.

[29] 74 ITD 1 (Ahd)
[30] 256 ITR 277

11. Recommendations

"The abuse of charities is becoming more organized and more sophisticated. Most countries surveyed by the OECD, have identified problems with the abuse of charities, and are having difficulties to detect all cases of abuse of charities and to quantify the risks associated with the abuse of charities for their respective tax administrations and the public in general. The electronic tax filing methods, including direct deposit refunds, used by tax administrations present significant challenges to quickly detect and deter the abuses of charities. It is essential for the tax authorities to implement or refine strategies to effectively address the risks of the abuse of charities.

11.1 Broad Recommendations for the Income-tax Authorities and assessing the impact of such recommendations in other parts of the world as per the OECD - Report on Abuse of Charities for Money-Laundering and Tax Evasion

It is recommended that tax administrations vulnerable to the risk of abuse of the charity sector consider implementing the following good practices:

- Maintain a central registry of all suspicious activities to identify and analyze trends;

  By establishing a centralized system for keeping data related to all suspicious activities related to abuse of charities and tax evasion plays an important role in identifying planned transactions and such data can be used in reporting and analysing the trends.

- Maintain reliable information on the real level of threat, vulnerability and compliance;

  By nominating various committees and statutory bodies, Government should assign the responsibilities to collect and maintain an exhaustive data related to charities and its utilization. Such data is to be processed and converted into useful information to identify the threat, vulnerable areas, and compliance statistics.

- Implement cross-functional teams;

  As per Canadian Tax Authority (CRA) the mandate of cross-functional teams consisted of:

  1) Working collaboratively in identifying suspicious activities while processing the 2007 T1 Income Tax and Benefit Returns (pre-assessment risk analysis);

2) Validating charitable donation claims (letters sent to 55 taxpayers requesting their receipts and proofs of payment);

3) Reacting to identified suspicious activity in a more timely manner; and

4) Conducting a more in-depth risk assessment of suspicious claims

- Implement an automated cross-check system;

  The Tax Authority for Canada is able to intercept the returns prior to their assessment and therefore avoided the subsequent use of resources to correct the situation and to recover the funds. The CRA Directorate responsible of administering tax law for charities has enhanced the compliance aspect of their administration of those tax laws through the use of risk assessment for audit and verification purposes.

  Further, the Revenue Agency of Italy has entered protocols of understanding with bodies operating in sectors related to non commercial entities in order to cross-check the information available (e.g. SIAE —Società Italiana Autori ed Editori - Central agency for the collection of copyright duties);

- Identify and develop relevant data sources;

  The Bank of Italy mandates financial intermediaries to examine carefully and promptly, every contractual relationship and operation which can be connected, directly or indirectly, with organizations that, while declaring that they carry out nonprofit, charitable or socially useful activities, are unable to provide supporting evidence.

- Exchange information and good practices on an ongoing basis;

  As a matter of good practice the tax authorities within the country and across the world should come forward to bridge information asymmetry amongst each other and educate themselves about the affairs of charities by mutual coordination and exchange of information on a regular basis.

- Input an “abuse of charities” indicator on suspicious files;

  In UK when abuse is identified or if there is a suspicion in specific areas legislation is introduced to stop the activity. Compliance efforts are risk based and better use is made of publicly available data on charities to target compliance efforts.

- Establish a mechanism to facilitate the exchange of information between tax authorities, law enforcement agencies, etc.

  In Turkey, in order to combat laundering of the proceeds of crime in a more effective way and prevent use of the financial system by criminals, certain obligations have been introduced for financial institutions and other professional organizations in both the international area and in domestic law. The information about the persons reporting suspicious transactions may not be given to third parties, institutions and organizations other than courts even if a provision exists in special laws. Necessary measures to be taken by the courts in order to keep secret the identities of the persons and to ensure their security.

Other Examples or results of successful activities designed to detect and address non-compliance

Belgium: Since the specialized CIT audit function has been put in place, this measure should make audits conducted on organizations liable for CIT and on registered organizations or organizations applying for registration, more consistent and more efficient.

Canada: The Canadian Tax Authority (CRA) conducted a pilot project prior to the last filing tax season (period of February 4, 2008 to March 28, 2008). The mandate of these cross-functional teams consisted of 1) working collaboratively in identifying suspicious activities while processing the 2007 T1 Income Tax and Benefit Returns (pre-assessment risk analysis) 2) validating charitable donation claims (letters sent to taxpayers requesting their receipts and proofs of payment); 3) reacting to identified suspicious activity in a more timely manner; and 4) conducting a more in-depth risk assessment of suspicious claims. The Tax Authority for Canada was able to intercept the returns prior to their assessment and therefore avoided the subsequent use of resources to correct the situation and to recover the funds.

Chile: Tax audits that have been executed during recent years show a low level of tax evasion related to charities.

Italy: No official estimates are available as of yet, however, the investigation activity concerning non-commercial entities and ONUS has increased over the past few years. For instance, in 2007, the Guardia di Finanza has assessed in this sector a tax evasion in direct taxation for an amount almost equal to the total amount assessed over the preceding three-year period (2003 to 2006).

UK: Some of the anti-avoidance legislation is too new to quantify any effect whilst other sections have been totally successful in stopping the abuse they were aimed at. Their compliance efforts with charities produced recoveries of around £15 million (€19 million) in the 2007 financial year. They cannot quantify recoveries from donors related to abuse of charity reliefs

although cases related to the gifts of assets will yield around £75million (€94 million) if they are successful. HMRC have also been successful in prosecuting individuals who have misused charities in order to evade taxes and make false repayment claims. Sentences ranged between 2 – 4 years and confiscation proceeding have been used in order to recover the proceeds of the criminal conduct. "[31]

11.2 Other Recommendations for amendments to the Income-tax Act, 1961

- Rampant misuse of section 2(15) as it's an inclusive definition and in the light of contrary judgments the said section needs a relook. The activities intended to be included need a thorough description and not be to cover for broad genre of activities.

  An exhaustive definition of charitable purposes should be introduced, in place of the present inclusive definition, to prevent too wide an interpretation. The charitable purposes could be exhaustively listed as set out in the Directive Principles of State Policy in the Constitution of India, wherever these mention any activity that is in the nature of service for advancement of public good. The list of purposes could also be updated periodically to address current needs. The definition of Charitable Purpose be made more specific and in tune with current nature of activities undertaken by the voluntary sector, while retaining the bar on commercial activities.

- The Shome Committee had earlier recommended that for eligibility for exemption, a charitable institution must have 90 percent of its receipts from donations alone. Below is an excerpt from the said report:

  "Under the IT Act, donations to NPOs are eligible for deduction under Section 80G and 80GGA from the gross total income. Since these are income-based deductions, these are iniquitous. Further, there has been a proliferation of NPOs in recent years. Numerous income tax exemptions in respect of their incomes are provided to them. Many of them are inefficient such as Sections 10(23)(i) to (iiia) and (iiiab) to (iiiae) since there is no bar imposed on the distribution of net earnings. They are also anomalous and, possibly, iniquitous in that NPOs enjoying exemptions under Sections 10(23)(iiiab) to (iiiae) coexist with for-profit organisations in their respective areas of operations.

  Also, the existing provisions produce tax subsidies that increase with income. Though Sections 11 to 13 do restrict distribution, they overlap with Sections 10 (23)(iv) to (via)

[31] Report On Abuse Of Charities For Money-Laundering And Tax Evasion – OECD

which do not restrict distribution. In any event, even if distribution of net earnings were restricted, there would be some inequity vis-à-vis for-profit enterprises because of the exemption itself. Further, no differentiation is made between donative and commercial NPOs. It is recommended that, first, the income-based deduction for donations under Section 80G and 80GGA should be converted to a tax credit at the lowest marginal tax rate of 10 percent—for equity reasons—without any limit as a fraction of gross income as set under Section 80G. Second, the exemptions under Section 10 and 11 to 13 of the Income-tax Act in respect of income of charitable Trusts and institutions of various categories should be restricted only to donative NPOs, to be defined as those in which 90 percent of the receipts are through donations.

Third, the non-distribution constraint should be made explicit and universal."[32]

- The provisions of section 10(23C) should be merged with those of sections 11, 12, 13 and 13A. That is to say, all charitable institutions seeking donations eligible for tax relief must submit to minimum discipline namely, obtaining initial approval, filing of returns annually and application of income and surpluses invested in specified ratios and channels. In judging the correct application of income by these entities, the existing anomalies arising from varying definition of "income" in the provisions governing charitable institutions should be removed.

"A number of questions on the charitable character of these organizations and institutions have been raised from time to time. Only 3 % of the assessees (51,570 Trusts) claimed 96 per cent (7,602,283 cr) of total deductions/exemptions. As Trusts are availing majority of total exemptions, the C&AG of India (hereinafter referred to as Audit) undertook Performance Audit on 'Exemption to Charitable Trusts and Institutions' to seek assurance on scheme of registration and assessment processes. The main objective of Audit's review was to seek assurance that registrations were given to Trusts involved in charitable activities only, and exemptions were allowed to eligible Trusts following are the observations of the Audit committee in their Performance Audit Report No. 20 of 2013:

Inconsistencies in the Income Tax Act, 1961

The Committee observed several inconsistencies in the IT Act such as there being no internal mechanism within Income Tax Department (ITD) to have control over the receipts issued by the entity having registration under section 80G. There is no provision in the Act to invest corpus fund in specified mode and tax interest earned thereon. The word "substantially financed" is not defined in Act. ITD in 30 cases allowed exemptions to

[32] Report of The Advisory Group on - Tax Policy and Tax Administration for the Tenth Plan.

Trusts who were claiming exemption benefit simultaneously/alternatively in both sections 10(23C) and 12A in different AYs. Audit also noticed deficiencies in Forms specified for Audit Report to be enclosed with the returns. In this regard, the Committee have been apprised by the Ministry that the Income Tax Act has been amended to provide that under section 11 and section 10(23C), income for the purpose of application shall be determined without any deduction or allowance by way of depreciation or otherwise in respect of any asset, acquisition of which has been claimed as application of income under these sections in the same or any other previous year. This amendment is effective from 1st April, 2015.

There is no provision under the Act to carry forward deficit. However, in view of adverse decisions of High Courts, the issue is under examination by the CBDT. In respect of issue of repayment of loan also, the suggestions are being examined in CBDT. The Committee would desire to be apprised of the latest position of the issues under examination of CBDT. The Committee are again perturbed to find that there is no enabling provision in the Act to disallow expenses on which TDS has not been deducted by Trusts similar to the Section 40 (a) (ia), applicable for the entities computing income under chapter IV. Further, statutory requirements imposed on Trusts like Audit Reports in Forms 10B or 10BB have no disclosure with regard to compliance with TDS provisions. However, according to the Ministry under the existing provisions of the Act the Trust is treated at par with the other deductors for non-compliance of the TDS provisions. No specific dispensation has been provided to the Trust deductors vis-à-vis other deductors. Further, with regard to making proper disclosure of TDS deducted/deductible in the Audit Report relating to a Trust assessee, the Committee have been apprised that at present the Audit Report relating to an assessee being a Trust does not contain a column for capturing such information. However, the Ministry has noted this suggestion. The Committee are of the opinion that only noting the suggestion would not suffice until this is adequately implemented. The Committee, therefore, recommended that appropriate provisions may be made for inclusion of such information in the Audit Reports of Trusts which as pointed out by Audit would be an effective tool for greater transparency during assessment procedures.

Delay in granting registration/approval/notification

Section 12AA of the IT Act/ Rule 11AA(6) of Income-tax Rules,1962, provides that Commissioner shall pass an order for registration/notification under section 12A/ 80(G) of the IT Act or reject the application within six months from the date on which such application was made. However, Section 10(23C) provides time limit for granting approval or rejecting the application within a period of 12 months from the end of the month in which such application is received.

The Committee are constrained to observe that in 594 Trust cases, IT Department delayed in issuance of registration/approval/notification after stipulated period of 6 or 12 months despite having clear provisions u/s 10(23C), 12A and 80G of the Act. The delay on the part of ITD resulted in deemed approval, to Trusts which were otherwise not eligible. The Committee are again perturbed to find that Income Tax Act is not explicit about the consequences/remedies available in case an application for ineligible Trusts is not processed with six months. The Committee are not inclined to accept the contention of the Ministry that the delay has taken place in exceptional cases as delays noticed in granting approval in 594 cases may not be exceptional. These might have been either due to procedural lapses or deficient internal control on the part of AOs for not adequately applying the provisions of the Act deliberately. The way deemed approvals have been granted by the Department in all these 594 cases make the Committee feel that there is certainly something amiss in the working of the IT Department which drastically needs to be streamlined. Therefore, they also desire that application seeking registration for Trusts must be disposed of expeditiously. Further, there are no reasons as to why provisions to this effect cannot be incorporated in the Act.

The Committee, therefore, desire that a serious thought needs to be given by CBDT in this regard. All cases where exemptions have been granted wrongly/illegally need to be probed with a view to fixing responsibility. The Committee have now been informed that restructuring of exemption Directorate would result in specialization on exemption matters with better control and monitoring. Further, proposal to make time barring limit uniform in respect of Section 12AA and 80 G applications by allowing extended time for completion in respect of Section 12AA applications by excluding time taken by applicants to comply with Commissioner's directions as available presently u/s 80 G is stated to be under examination of CBDT. The Committee have further been informed that the feasibility of introducing web based interactive platform for applying for registration, submitting soft copy of necessary documents and communicating with each other thus making the whole process faster, smoother, transparent and less time consuming is under discussion in CBDT. The Committee would like the Ministry to undertake these proposed measures expeditiously with a view to avoid delay in granting registration/approval/notification."[33]

- Giving deductions u/s 80G for corporates needs a re-look just as CSR is not a deductible expenditure. Though the impact of tax revenue forgone is not very significant a relook at the existence of this section is necessary on par with CSR for corporate**.**

[33] TWENTY SEVENTH REPORT PUBLIC ACCOUNTS COMMITTEE (2015-16) (SIXTEENTH LOK SABHA) EXEMPTIONS TO CHARITABLE TRUSTS AND INSTITUTIONS MINISTRY OF FINANCE DEPARTMENT OF REVENUE Presented to Lok Sabha on: 16.12.2015
PAC No. 2059

Statement of Revenue Impact of Tax Incentives under the Central Tax System Financial Years 2015-16 and 2016-17:

Deduction on account of donations to charitable Trusts and institutions (section 80G	Revenue Impact in Crore) [2015-16]	Projected Revenue Impact (in Crore) [2016-17]
For corporate tax payers	1275.9	1386.0
For non-corporate [Firms/AOPs/BOIs] tax payers	105.3	114.4
For individual/HUF tax payers	486.3	595.15
Total	**1867.5**	**2095.55**

Source: Annexure 13 of Receipt Budget (2017-18) (indiabudget.gov.in)

The reporting structure on tax revenue foregone should be more detailed and comprehensive. A mere report on amounts of tax revenue foregone, does not add much value to the process.

Government's policy of exempting income of charitable institutions plays a significant though not clearly quantified role in securing momentum for economic growth. In the same vein, it is indicated that this policy is substantially reducing the fiscal space and is therefore a serious challenge to revenue mobilization. Given the double-edged nature of tax incentives and exemptions, a comprehensive study on the costs and benefits that have accrued from these tax exemptions and deductions is unavailable. The number of anti-avoidance measures embedded in the Act proves the abuse of the existing tax regime.

- "Voluntary organizations receiving more than Rs 11,500 crore ($1.9 billion) in foreign funds annually, the Home Ministry has warned that the NGOs could be vulnerable to risks of money laundering and terror financing. A total of 43,527 NGOs are registered under the Foreign Contribution (Regulation) Act, as of March 31, 2012."[34] An amendment to the Prevention of Money Laundering Act (PMLA) 2002, notified in the Official Gazette to bring NPOs under the purview of the law. A law on charities should be framed which includes provisions for Anti-Money Laundering and Anti-Terrorist Financing and

[34] Money laundering Through Indian NGOs – By Mayur Joshi *(Indiaforensic.com)*

Reporting. A Risk Based Approach - the greater the risks, more the Trustees have to do to ensure that they have discharged their duty and other legal duties.

- There is another element of the charitable deduction many find problematic: it consistently favors the wealthy, making it "cheaper" to give if you have more money than less. At the heart of the issue is also a debate about the role of Govt. versus philanthropy—which is better at delivering critical social services?

12. Conclusion

The rationale for exempting the income of charitable institutions or allowing deduction for donations to charities is definitely a question which the policy makers need to fundamentally look at along with reviewing the tax treatment of charities considering that it has been a source of worry for tax administrators and policymakers everywhere.

The main reason is that there is a widespread feeling that the cover of exemption is often used to promote private gain and not always or entirely for charitable objectives. Hence tax laws invariably stipulate safeguards to ensure that the concessional treatment of charitable institutions is not misused. The strategy followed for this purpose mainly has been to define charity in such a manner that the scope for using tax exemptions for profit making is minimised, if not eliminated and to lay down specific conditions to be met by a charitable institution seeking exemption. Provisions in this regard have been in force in the Indian income tax since long. But these have undergone many changes over the years, partly as a result of court rulings and partly to meet the requirements of an evolving society. In operation, however, these changes are found to have certain weaknesses which tend to undermine the efficacy of the safeguards meant to ensure that the benefit of tax exemption goes only to genuine charities.

The weaknesses stem partly from the inadequacies of the definition of charitable purpose and also the ambivalence of the law in dealing with different types of charitable institutions.

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Money laundering Through Indian NGOs – By Mayur Joshi *(Indiaforensic.com)*

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