

# TAXATION CHARITABLE TRUST

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# Structure of a Non Profit Organization in India

In India non profit organizations can be registered as:



- ❖ The Income Tax Act gives all categories equal treatment, in terms of exempting their income and granting 80G certificates, whereby donors to non-profit organizations may claim a rebate against donations made. Foreign contributions to non-profits are governed by FC(R)A regulations and the Home Ministry

# Comparison among Trust, Society & Section 8 Company

Points of Differences	Trust	Society	Section 25 Company
Statute / Legislation	Relevant State Trust Act or Indian Trust Act, 1882	Societies Registration Act, 1860	Indian Companies Act, 1956
Jurisdiction	Deputy Registrar/Charity commissioner	Registrar of societies (charity commissioner in Maharashtra).	Registrar of companies
Registration	As trust	As Society In Maharashtra, both as a society and as a trust	As a company u/s 8 of the Indian Companies Act.
Registration Document	Trust deed	Memorandum of association and rules and regulations	Memorandum and articles of association. and regulations
Stamp Duty	Trust deed to be executed on non-judicial stamp paper, vary from state to state	No stamp paper required for memorandum of association and rules and regulations.	No stamp paper required for memorandum and articles of association.
Members Required	Minimum – two trustees. No upper limit.	Minimum – seven managing committee members. No upper limit.	Minimum three .No upper limit.
Board of Management	Trustees / Board of Trustees	Governing body or council/managing or executive committee	Board of directors/ Managing committee
Mode of Succession on Board of management	Appointment or Election	Appointment or Election by members of the general body	Election by members of the general body

## Method of Computation of Income

- ❖ Income from the properties of the trust have been held to be arrived at in the normal commercial manner without classification under the various heads set out in section 14 (CIT Vs. Rao Bahadur Calavala Cunnan Chetty Charities (1982) 135 ITR 485 (Mad))
- ❖ Real income has to be taken into account for the purpose of considering the exemption u/s 11 (CIT Vs. Birla Janhit Trust (1994) 208 ITR 372, 375-76 (Cal))

## Method of Computation of Income

- ❖ In that view of the matter, the loss incurred by the charitable trust on sale of investment is not allowable in computing the income of the trust because of the fact that such loss can not formed part of the real income of the trust. (Hindustan Welfare Trust Vs. Director of Income Tax (exemption) (1993) 201 ITR 564, 566)
- ❖ It may also be noted that where provisions of section 11 are attracted, the provisions of section 28(iii) cannot be invoked. [CIT Vs. South Indian Film Chamber of Commerce (1981) 129 ITR 22 (Mad)]

# Income of Trust exempted under Section 11

Section	Nature of income	Extent to which exemption allowed
11(1)(a)	Income derived from property held under trust wholly for charitable or religious purposes	To the extent income is applied to such charitable or religious purposes in India.  Whereas such income is accumulated or set apart for such application, to the extent of 15% of the income from such property.
11(1)(c)	Income derived from property held under trust for a charitable purpose, which tends to promote international welfare in which India is interested	To the extent income is applied to such charitable or religious purposes outside India.  Exemption is available only if the Board has directed such exemption.
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.	100% exemption.

In computing the 15% of the income which may be accumulated or set apart, any such voluntary contributions as are referred to in Section 12 shall be deemed to be part of the income.

# No exemption under Section 11

## Section

## Nature & extent of income not exempt under Section 11

13(1)(a)

Income of private religious trust not used for public benefit.

13(1)(b)

Income of charitable trust created for benefit for particular religious community.

13(1)(c)

Income/ property of charitable or religious trust applied for direct or indirect benefit of person referred in 13(3)

13(1)(d)

Any income, is taxable if

If any funds are invested other than in 11(5)

Any funds invested earlier than 1983 remain invested thereafter

Shares and company are held after 1983.

11(4A)

Income from business which is not incidental to the attainment of the objectives of the trust, or in respect of which separate books of accounts have not been maintained.

12(2)

Value of medical/ education services provided to specified persons by trust running hospital and educational institution shall be income of trust and will be chargeable in the year in which services are provided and chargeable to tax, despite section 11(1).



## Conditions subject to which income derived from property held under trust is exempted under section 11

- ❖ Trust must have been created for any **lawful purpose**. The trust should not be created for the benefit of any particular religious community or caste.
- ❖ The trust should be **registered** with the Commissioner of Income Tax under Section 12A
- ❖ The property from which income is derived should be **held under a trust** by such charitable or religious trust / institution. The property should be held wholly for charitable purposes.
- ❖ The exemption is confined to only **such portions** of the trust's income which is applied to charitable or religious purposes or is accumulated for applying to such purposes in India.
- ❖ **85% of the income is required to be applied** for the approved purposes and the unapplied income and the money accumulated or set apart (in excess of 15% of the income from such property) should be invested in the specified forms or modes.
- ❖ **No part of the income should ensure**, directly or indirectly, for the benefit of the settler or other specified persons.



# Concept of 'Corpus'

- ❖ There is **no judicial guidance** on the subject as to what amount in the funds of a trust will constitute its corpus.
- ❖ According to Black's Law Dictionary, it means "an aggregate or mass; physical substance, as distinguished from intellectual conception; **the principal sum or capital, as distinguished from interest or income**; the main body or principal of a trust."
- ❖ The corpus ingredient constituted of the originally donated or settled capital amount in the form of money, movable property or immovable property (which might conveniently be termed as original corpus) plus any contribution received by the trust with a specific direction that it shall form part of the corpus of the trust.
- ❖ To claim a donation to be a corpus donation it is necessary that a written direction from donor is obtained.

# Voluntary Contributions received by a Trust

- ❖ The voluntary contributions received by a charitable or religious trust are to be treated as follows:

- ✓ Corpus Donations

Voluntary contributions made to a charitable or religious trust with a specific direction that they shall form part of the corpus of the trust i.e corpus donations **do not form part** of the total income of the trust as per Section 11(1)(d).

- ✓ Contributions other than corpus donations

Section 12(1) states that any voluntary contributions (not being corpus donations) received by a charitable or religious trust shall be deemed to be the **income derived from property held under trust** wholly for charitable or religious purposes. Such voluntary contributions would therefore be eligible for exemption under Section 11(1) provided the trust satisfies the conditions as prescribed under Section 11 and 13.

- ❖ **While corpus donations do not form part of total income, other voluntary contributions are exempt from tax as per Section 11 and 13**

# Voluntary Contributions received by a Trust

- ❖ Membership fees or subscriptions cannot be treated as voluntary contribution as they are not the gratuitous payment by the member for any social purpose or a payment without any constitution.

**[Trustee of Shri Kot Hindu Stree mandal v. CIT [1994] 209 ITR (Bom.)]**

- ❖ Where a trust received voluntary contribution with specific direction that it should form a part of the trust corpus, the trust will not lose exemption if the contribution is applied for meeting running expenses.

**[Dharma Pratishthanam v. ITO [1985] 11 ITD 40 (Delhi)]**

- ❖ Where a charitable trust received donations from different donors who had specifically directed that the donations were to remain as corpus of the trust, the trust will not be precluded from using those receipts for making donations to other charitable trusts. Section 12 does not recognize such receipts as income of the trust for the purpose of Section 11.

**[ITO v. Abhilash Kumari Public Charitable Trust [1987] 28 TTJ 523 (Delhi)]**

## Application of Income

- ❖ The exemption under Section 11 is available only if the income derived from property held under trust is 'applied' to the charitable or religious purposes.
- ❖ Income must be available for application. TDS cannot be considered as income. **CIT V. Jayshree Charity Trust 1985 Tax LR 247 (Cal)**
- ❖ The application of income need not necessarily result in expenditure. Therefore, an amount irretrievably earmarked or allocated for the purposes of the trust or institution is also treated as applied even though it has not been actually spent. **[CIT Vs. Trustees of the HEH Nizams Charitable Trust (1981) 131 ITR 497 (AP)]**
- ❖ Application need not necessarily result in revenue expenditure. Even capital expenditure is considered to be application of income for the purposes of Section 11 if it is incurred for charitable purposes. **[CIT v. Kannika Parameshwari Devasthanam & Charities [1982] 133 ITR 779 (Mad.)]**

# Conditions Of Accumulation

- ❖ 11(2): Accumulation of unapplied income.
- ❖ 11(2)(a): Application for accumulation upto 5 years.
- ❖ 11(2)(b): Accumulated income to be invested as per 11(5)
- ❖ *Proviso-1*: Period of stay from court to be excluded in calculating 5 years.
- ❖ *Proviso-2*: 10 years to be substituted 5 years in case of income accumulated after 1-4-2001.
- ❖ *Explanation*: Accumulation for benefit of exempted institutions u/s 12AA and 10(23) shall not be treated as application.

# Conditions of Accumulation

- ❖ **Section 11 (2) not to restrict operation of section 11(1)**

✓ In the case of **Addl. CIT Vs. A.L.N. Rao Charitable Trust (1995) 216 ITR 697 (SC)**, it is been held that accumulated income which is exempt under section 11(1)(a) need not be invested in Government Securities.

- ❖ **Belated Applications For Accumulation**

- ❖ CIRCULAR NO. 273

The board has passed a general order U/S 119(2)(b) – No.180/57/80-IT(AI) by which the CIT has been authorized to admit belated applications U/S 11(2) r/w r.17 of the IT rules if certain conditions are satisfied.



## Taxability Of Accumulated Income – in which year?

- ❖ 11(3)(a): Applied for purposes other than charity or ceases to be accumulated or set apart for charity – **taxed in such year of application.**
- ❖ 11(3)(b): Ceases to be invested in 11(5) – **taxed in year of cessation.**
- ❖ 11(3)(c): Is not utilized for the purpose for which it was accumulated, by the expiry of the year immediately following the period of accumulation – **taxed in year immediately following expiry** of period aforesaid.
- ❖ 11(3)(d): Is credited or paid to exempted trust – **taxed in year of credit or payment.**



## Application To Change Purpose Of Accumulation

- ❖ 11(3A): In case of 11(2), if the income can not be applied for the purpose for which it was allowed to be accumulated, then an application can be made to change the purpose of accumulation.
- ✓ Proviso 1: The changed purpose can not be for payment to exempted trust.
- ✓ Proviso 2: Accumulated funds of dissolved trust can be credited or paid to exempted trust in the year the accumulating trust was dissolved.

# Treatment of capital gains

- ❖ Section 11(IA) first caters to two main situations, viz.
  - ✓ where the capital asset is property held under a Trust wholly for charitable or religious purposes;
  - ✓ where the capital asset is held under a Trust in part only for such purposes
- ❖ Within these main situations, the provision also caters to the following sub situations:
  - ✓ where the whole of the net consideration is utilized in acquiring the new capital asset;
  - ✓ where only a part of the net consideration is utilized for acquiring the new capital asset.
- ❖ In respect of each of these sub-situations under the main situations, the section spells out the quantum of income which will be deemed to have been applied to charitable or religious purposes.

# Treatment of capital gains

- ❖ 'Income', as defined under section 2(24), includes Capital Gains,. Therefore, for the purposes of section 11(1)(a), Capital Gains are also considered as a part of the income. Since, Capital Gains are also considered as a part of the income, therefore, they can be applied for charitable or religious purposes.
- ❖ Under section 11(1A), if the entire amount of net consideration is invested in another Capital Asset then, the entire Capital Gain will be deemed to have been applied for Charitable or Religious purposes.
- ❖ Under section 11(1A), if a part of the entire amount of net consideration is invested in another Capital Asset then, the appropriate fraction of the Capital Gain will be deemed to have been applied for charitable or Religious Purposes.

# Treatment of capital gains

- ❖ The Capital Gain have to be re-invested in another Capital Asset in the same year, unless the assessee exercises the option available under explanation to section 11(1), to apply the income in subsequent year.
- ❖ Investment in fixed deposit is considered as an investment in Capital Asset. The CBDT instruction no. 883, dated 24.09.1975, specifies that, such fixed deposits should be for 6 months or more. But, various High Courts have held that, such 6 months time limit is legally not valid. The nature of asset is important and not the time frame.
- ❖ No time limit has been provided under section 11(1A), for retention of the new asset. Under the prevailing provisions each year's income and application are treated separately for the purposes of exemptions. Therefore, if the asset is held till the end of the relevant previous year and is disposed of in the subsequent year, then the exemptions cannot be denied nor can they be withdrawn in the next year.

# Treatment of capital gains

## Illustration I

The following illustration clarifies the treatment of capital gains under section 11(IA).

Cost of the Asset	Rs. 40,000/-
Sale Proceeds/Net consideration	Rs. 1,00,000/-
Re-investment in Capital Assets	(i) Rs. 80,000/- (ii) Rs. 1,00,000/-

## Solution I

The computation of capital gain deemed to have been applied for the purposes of section 11(1)(a) is as under :

(i) Net consideration		1,00,000	1,00,000
(ii) Cost of the Asset		40,000	40,000
(iii) Capital gains	60,000		60,000
(iv) Investment in New Asset	80,000		1,00,000
(v) Shortfall in re-investment (i) - (iv)		20,000	Nil
(vi) Capital gains deemed to have been applied for charitable purposes (iii) - (v)		40,000	60,000

# Business Income of a Trust

- ❖ Section 11(4) provides that a business undertaking held by a trust will be treated as a property held under a trust.
- ❖ Where a claim is made that the income of any business shall not be included in the total income, the AO shall have the power to determine the income of such undertaking in accordance with the provisions of the Act relating to the assessment. (i.e. as per Section 28 to 44 )
- ❖ Where any income so determined is in excess of the income as shown in the accounts of the undertaking such excess shall be deemed to be applied to purposes other than charitable or religious purposes and thus, it will be liable to be taxed accordingly.

# Business Income of a Trust

- ❖ As per Section 11(4A), the income earned by a trust from any business activity shall be exempted from tax provided the following conditions are satisfied:
  - ✓ The business carried on is incidental to the attainment of the objects of the trust and
  - ✓ Separate books of accounts are maintained in respect of such business
- ❖ It has been held in [CIT v. Thanthi Trust [2001] 247 ITR 785 (SC)], that a business whose income is utilized by the trust for the purpose of achieving the objectives of the trust is, surely, a business, which is incidental to the attainment of the objectives of the trust. In any event if there is an ambiguity, the provision must be construed in a manner that benefits the assessee.



# Rental Income of a Trust

- ❖ Rent derived from additions to trusts buildings is exempt from tax when rent was used for religious purposes.
- ❖ The words applied is wider in import than the word expenditure. Expenditure means disbursement, paying out, distribution or spending. The money or amount will not go out irretrievably when it is applied to a purpose. The construction of the building was for the purpose of getting some income by way of rent and such income would be applied to the charitable or religious purposes. The purpose was sufficient for satisfying Section 11(1).

**[CIT v. St. George Forana Church [1988] 170 ITR 62 (Ker.)]**

# Rental Income of a Trust

- ❖ It has been held that letting of Dharamshala's , auditoriums, running of libraries, etc. could not be considered as business activities and any income generated from such activities should be considered as income from properties held under trust . In **CIT Vs. Ganesh Ram Laxminarayan Goel (1984) 147 ITR 468 (MP)**, it was held that letting out of dharamshala's was an activity towards attainment of the objects of the organisation and profit making was not the profit motive and therefore it could not be considered as business activity.

## Section 13 (1)(a)

- ❖ The exemption under the head religious trusts has always been available only in respect of religious trusts which enure for the benefit of the public.
- ❖ Where the trust is for private religious purposes, the exclusion did not and does not apply to that part of the income from property held under trust which does not enure for the benefit of the public.

**[CIT v. Bengal Mills & Streamers Presbyterian Assn [1983] 140 ITR 586 (Cal.)]**

## Section 13(1)(b)

- ❖ This section enacts that income of a trust or charitable institution created or established after 1.4.1962 for the benefit of any particular religious community or caste is not excluded from its total income.

**In [CIT v. Shri Maheshwari Agarwal Marwari Panchayat [1982] 136 ITR 556 (MP)]** it was held that since the trust was for a particular religious community, the provisions of section 13(1)(b) were not applicable as they apply only to charitable trusts. As per this interpretation, 13(1)(b) will not apply in case of religious or both Religious & charitable trusts.

## Section 13(1)(c)

- ❖ Where a part of income of the charitable or religious trust or institution is used or applied, directly or indirectly, for the benefit of the settlor, founder and certain other specified persons is not eligible for exemption.

**[Director of income tax v. Bharat Diamond Burse [2003] 259 ITR 280 (SC)]**

## Section 13(1)(d)

- ❖ The income of any charitable or religious trust will not be entitled to exemption under section 11 or 12 if, for any period during the previous year:
  - ✓ Any funds of the trust are invested after 28.02.1983, otherwise than in any one of more of the forms specified in 11(5);
- ❖ In [CIT v. ALN Rao Charitable Trust [1995] 216 ITR 697 (SC)], it was held that accumulated income which is exempt u/s 11(1)(a) need not be invested in the Govt. Securities; it is only in respect of any additional accumulated income beyond 15% that, if the assessee wants exemption of its additional accumulated income also, the assessee is required to invest the additional accumulated income in the manner laid down in section 11(5)

# Anonymous Donations

- ❖ Anonymous donations of the following entities shall be included in the total income u/s 115 BBC and taxed at the rate of 30%.
  - (i) any trust or institution referred to in section 11;
  - (ii) any university or other **educational** institution referred to in section 10(23C)(iiiad) and (vi) i.e. its annual receipts is less than or more than Rs. 1 crore;
  - (iii) any **hospital** or other institution referred to in section 10(23C) (iii a e) and (vi a) i.e. its annual receipts is less than or more than Rs. 1 crore;
  - (iv) any fund or institution referred to in section 10(23C)(iv); (established for **charitable** purpose)
  - (v) any trust or institution referred to in section 10(23C)(v). (established for public religious purposes or **public religious & charitable purposes** )



# Anonymous Donations

- ❖ *Anonymous donations not covered under section 115BBC*

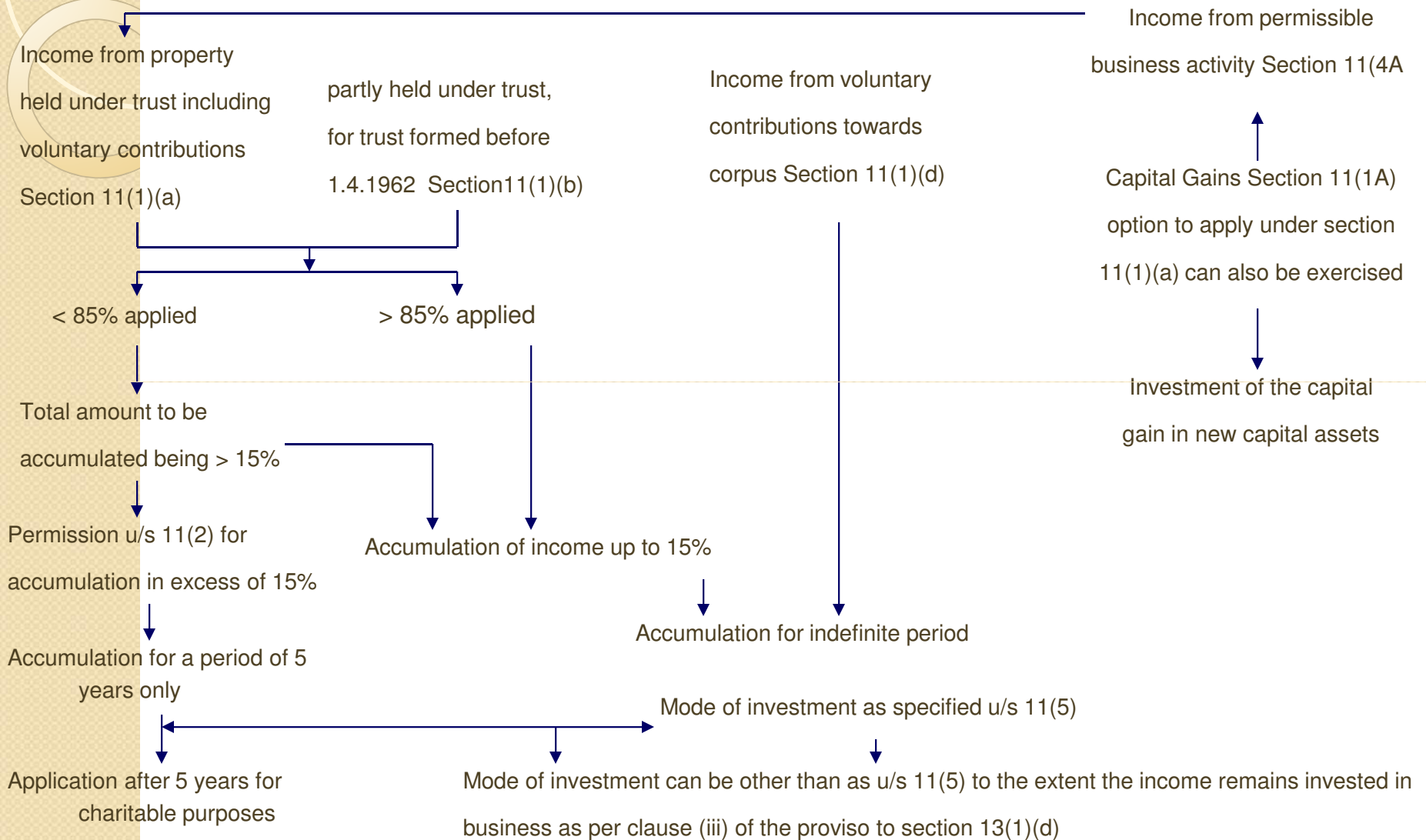
The following anonymous donations shall, however, be not be covered under section 115BBC:

(a) donations received by any trust or institution created or established **wholly for religious purposes**.

(b) donations received by any trust or institution created or established for **both religious as well as charitable purposes** (other than any anonymous donation 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.)

- ❖ The term "anonymous donation" is defined to mean any voluntary contribution, where the person receiving such contribution does not maintain a record consisting of the identity of the person making such contribution indicating the name and address of the person and such other particulars as may be prescribed. Such anonymous donations will be taxed @ 30% (to be increased by surcharge as applicable and education cess.)

# Birds eye view of provisions of section 11



## Taxability of a Public Trust at a glance

Sources of Income	Under Section	Tax Rates
Voluntary Contributions (being corpus donations)	11(1)(d)	Exempt
Income not applied / accumulated to the extent > 15%	11(1)(a)	AOP Rate
Income received on 31 <sup>st</sup> March carried forward to next year for utilization but not utilized in that next year [Explanation 2(b) to Section 11(1)(d)]	11(1B)	AOP Rate
Income accumulated u/s 11(2) is not invested / utilized / donated to another trust	11(3)	AOP Rate
Excess Business Income as assessed by the AO	11(4)	AOP Rate
Income derived u/s 13(1)(a) & 13(1)(b)		AOP Rate
Income derived u/s 13(1)(c) & 13(1)(d)		MMR
Anonymous Donations u/s 115BBC		30%

# Taxability of Public Trust

## Taxability of Public trusts

Income is not exempt u/s 11 or 12

Section 164(2)

Taxable at the rates applicable in  
case of AOP

Exemption u/s 11 or 12 is forfeited  
due to contravention u/s 13(1)(c) or  
13(1)(d) Section 164(2)

Taxable at the Maximum Marginal rate

## Tax rates applicable to Public Charitable or Religious Trust


- ❖ Where income is not exempt under section 11 or 12 [Section 164(2)]  
Taxable at the rates applicable in case of an AOP
- ❖ Where exemption under Section 11 or 12 is forfeited due to contravention under Section 13(1)(c) or 13(1)(d) [Section 164(2)]  
Such income is taxable at maximum marginal rate.

However, in the case where the assessee is not entitled to exemption under Section 11 or 12, by virtue of the provisions contained in Section 13(1)(b), the maximum marginal rate does not become applicable. The income will then be charged on rates specified for an association of persons as provided under Section 164(3)

**[ITO v. Gurjar Pushkarna Vidyotejak Mandal [1988] 30 TTJ 610 (Ahd.)]**

## Tax rates applicable to Public Charitable or Religious Trust

- ❖ A trust will attract MMR of tax only on that part of the income which has forfeited exemption under the above circumstances and not on the entire income of the trust.- **Director of Income tax ( Exemption) V. Sheth Mafatlal Gagalbhai Foundation Trust (2001) 114 Taxmann 19 ( Bom)**
- ❖ In **Gurdayal Berlia Charitable Trust V.fifth Generation Trust v. fifth ITO (1990) 34 ITD 489, Bombay**, the tribunal observed that only the income from unapproved investment would be Taxable at MMR.



***Thank You***  
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