

Income Which do not Form Part of Total Income

Some Key Points : Recent Amendments

Increase in monetary limit in respect of permissible receipts from trading activity for an institution with the object of “advancement of any other object of general public utility” to retain its “charitable” status [Section 2(15)]

The Finance Act, 2011 has increased the limit in respect of permissible receipts from trading activity for an institution with the object of “advancement of any other object of general public utility” from ₹ 10 lacs to ₹ 25 lacs w.e.f. A.Y.2012-13. Therefore, in effect, “advancement of any other object of general public utility” would continue to be a “charitable purpose”, if the total receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed ₹ 25 lakhs in the relevant previous year.

Exemption of specified allowances and perquisites paid to Chairman or a retired Chairman or any other member or retired member of the UPSC [Section 10(45)]

New clause (45) has been inserted in section 10 by the Finance Act, 2011, effective retrospectively from A.Y. 2008-09, to exempt specified allowances and perquisites (as notified by the Central Government) received by Chairman or any other member, including retired Chairman/member, of the Union Public Service Commission (UPSC).

Exemption of specified income of notified entities not engaged in commercial activity [Section 10(46)]

- (i) New clause (46) has been inserted in section 10 by the Finance Act, 2011, effective retrospectively from 1st June, 2011, to provide for exemption of income arising to a body or authority or Board or Trust or Commission, the nature and extent of which is to be specified by the Central Government.
- (ii) For availing the benefit of exemption under this clause, the body or authority or Board or Trust or Commission should be set up or constituted by or under a Central, State or Provincial Act or constituted by the Central or State Government with the object of regulating or administering an activity for the benefit of the general public.
- (iii) Further, the body or authority or Board or Trust or Commission should –
 - (1) not be engaged in any commercial activity;
 - (2) be notified by the Central Government in this behalf.

Exemption of income of notified infrastructure debt funds and concessional tax rate on interest received by non-residents from such fund [Section 10(47)]

In order to give a fillip to infrastructure and encourage inflow of long-term foreign funds to this sector, the Central Government to notify infrastructure debt funds to be set up in accordance with the prescribed guidelines, the income of which would be exempt from tax w.e.f. 1st June, 2011.

VRS Compensation [Section 10(10C)]

When VRS compensation is received by an employee, he would be eligible to claim either exemption under section 10(10C) or relief under section 89. The assessee cannot opt to claim both the benefits viz. exemption under section 10(10C) and relief under section 89. The tax relief is limited to any one benefit, as may be chosen by the assessee.

Relief to Scientific Research Association [Section 10(21)]

A scientific research association approved and notified under section 35(1)(iii) is eligible to claim exemption under section 10(21). The object of the association however must be undertaking research in social science or statistical research. Even income from business of the scientific research association is eligible for exemption provided the business is incidental to the attainment of its objectives and separate books of account are maintained in respect of such business.

Cancellation of registration [Section 12A]

Section 12A was amended by the Finance (No.2) Act, 1996. The law did not empower the Commissioner to cancel registration in respect of trusts or institutions which were registered prior to the said amendment. The Finance Act, 2010 has amended section 12AA(3) to empower the Commissioner to cancel registration in respect of any trust or institution which was registered at any time under section 12A before the amendment was brought in by the Finance (No.2) Act, 1996.

Electoral Trust [Section 13B]

The term 'electoral trust' is defined in section 2(22AAA) which means a trust so approved by the Board in accordance with the scheme made in this regard by the Central Government.

As per section 13B any voluntary contribution received by an electoral trust shall not be included in the total income of the previous year of such electoral trust, if –

- (a) such electoral trust distributes to any political party, registered under section 29A of the Representation of the People Act, 1951, during the said previous year, ninety five percent of the aggregate donations received by it during the said previous year along with the surplus, if any, brought forward from any earlier previous year; and
- (b) such electoral trust functions in accordance with the rules made by the Central Government.

It may be noted that donations given by assessee to electoral trusts are eligible for deduction under sections 80GGB and 80GGC of the Act in computing the total income of the donor.

Question 1

- (A) Mr. Ramanand, after putting 25 years of service, opted for voluntary retirement and under approved scheme received an amount of ₹ 20 lacss as VRS compensation on 01.01.2012. He was advised by his tax consultant to claim exemption to the extent as specified in section 10(10C) and also the relief under section 89. He, in order to have an expert opinion, consults you and asks whether such a treatment of VRS compensation is permissible under the Act.
- (B) Which are the conditions to be satisfied by an electoral trust for claiming the benefit of exemption of its income? Is this benefit available in respect of all the income earned by an electoral trust?
- (C) Mr. Divyam avails the benefit of LTC and went by air (economy class) on a holiday in India on 25.01.2012 along with his wife and three children consisting of son aged 4 years and twin daughters of 1 year age. Total cost of tickets reimbursed by his employer was ₹ 90,000 (₹ 60,000 for 2 adults and ₹ 30,000 for the three children). State with reasons the amount which can be claimed by Mr. Divyam out of the reimbursement as not subject to tax. Will your answer be different where among his three children the twins were of 4 years of age and the age of the son was of 1 year?

Answer

- (A) Where any relief was allowed under section 89 for any assessment year in respect of any amount received or receivable on voluntary retirement, no exemption under section 10(10C) shall be allowed in respect of the said sum in that assessment year or any other assessment year.

Similarly, relief under section 89 cannot be claimed if benefit of exemption has been claimed under section 10(10C).

Mr. Ramanand can, therefore, opt to claim exemption of ₹ 5 lacs under section 10(10C) or relief under section 89(1) in respect of compensation received on voluntary retirement, but not both. Accordingly, the advice given by his tax consultant is not correct.

- (B) An approved electoral trust is eligible for exemption under section 13B in respect of voluntary contributions received by it.

The voluntary contributions received by such electoral trust shall be treated as its income under section 2(24), but shall be exempt under section 13B, if the electoral trust:-

- (i) distributes to a registered political party during the year, 95% of the aggregate donations received by it during the year along with the surplus, if any, brought forward from any earlier previous year.
- (ii) functions in accordance with the rules made by the Central Government.

The benefit under section 13B is available only in respect of voluntary contribution received by an electoral trust and not in respect of its other income

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- (C) Mr. Divyam can avail exemption as per section 10(5) on the entire amount of ₹ 90,000 reimbursed by the employer for the LTC as the same was availed for himself, his wife and the three children in India and the journey was also undertaken by economy class airfare. The restriction imposed for two children is not applicable to the multiple births which take place after the first child.

However, if the age of the twin daughters is more than the age of the son, the restriction imposed for two children under the section would be applicable and therefore, Mr. Divyam cannot avail exemption in this case for all the three children. The exemption of LTC can be availed in respect of only two children. Therefore, the fare of ₹ 10,000 (i.e., ₹ 30,000 × 1/3) reimbursed for one child will form part of taxable salary and balance amount of LTC of ₹ 80,000 (90,000 - 10,000) will be exempt under section 10(5).

Question 2

If an assessee does not claim any expenditure with respect to exempt income then write down the prescribed methods that the Assessing Officer would follow to determine the amount of expenditure incurred in relation to exempt income.

Answer

If the assessee claims that no expenditure has been incurred by him in relation to exempt income, the Assessing Officer shall proceed to determine the amount of expenditure incurred in relation to such exempt income in accordance with the method prescribed in Rule 8D.

Rule 8D lays down the method for determining amount of expenditure in relation to income not includible in total income.

If the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with –

- (a) the correctness of the claim of expenditure by the assessee; or
- (b) the claim made by the assessee that no expenditure has been incurred in relation to exempt income for such previous year,

he shall determine the amount of expenditure in relation to such income in the manner provided hereunder -

The expenditure in relation to income not forming part of total income shall be the aggregate of the following:

- (i) the amount of expenditure directly relating to income which does not form part of total income;
- (ii) in a case where the assessee has incurred expenditure by way of interest during the previous year which is not directly attributable to any particular income or receipt, an amount computed in accordance with the following formula, namely :

$$A \times \frac{B}{C}$$

Where,

- A = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year;
- B = the average of value of investment, in relation to income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;
- C = the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;
- (iii) an amount equal to one-half per cent of the average of the value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.

'Total assets' means total assets as appearing in the balance sheet excluding the increase on account of revaluation of assets but including the decrease on account of revaluation of assets.

Question 3

An electoral trust approved by the Central Board of Direct Taxes is not liable to income-tax in respect of voluntary contribution received and other income - Discuss the correctness of the statement.

Answer

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

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

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

Therefore, the given statement is not correct.

Question 4

Can the provisions of section 14A of the Income-tax Act, 1961 be applied for disallowing expenditure relating to income for which deduction is available under Chapter VIA, or the section can be invoked only in respect of expenditure relating to income exempt under the provisions of section 10?

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Answer

Chapter III, comprising sections 10 to 13B, deals with incomes which do not form part of total income. As per section 14A(1), for the purposes of computing the total income under Chapter IV, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under the Income-tax Act, 1961. Therefore, from a plain reading of section 14A, it is apparent that the intention of the section is to disallow expenditure in relation to income which does not form part of total income i.e., expenditure in relation to income exempt under section 10 to 13B.

Therefore, the provisions of section 14A cannot be applied for disallowing expenditure relating to income for which deduction is available under Chapter VIA.

Question 5

An educational institution having annual receipts of ₹ 1.20 crore during the P.Y.2011-12, has to make an application to the prescribed authority before 31.3.2012 for claiming tax exemption under section 10(23C). Discuss the correctness or otherwise of this statement.

Answer

This statement is not correct.

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

Therefore, in the given case, the educational institution (having annual receipts of ₹ 1.20 crore during the P.Y.2011-12) can make an application for grant of exemption in the prescribed form to the prescribed authority on or before 30th September, 2012.

Question 6

Ankur, the owner of a land situated in Kerala used for growing thereon different types of fruits, paddy, vegetables and flowers, received from Yahoo Movies Ltd., Chennai, ₹ 5 lacs as rent towards the use of this land for shooting of a film. The amount so received was accounted by him in the books as revenue derived from land and claimed to be exempt under section 10(1). He now wants to confirm from you whether the amount has been correctly treated by him as agricultural income.

Answer

The income received by Mr. Ankur from a filmmaker for allowing them to shoot a film in the agricultural land owned by him is not in the nature of agricultural income because it was neither received by him against the sale of agricultural produce obtained nor for carrying out the normal agricultural operations on the land. The amount paid was only for the purpose of shooting of a film on such land.

To claim exemption for agricultural income under section 10(1), the conditions contained in section 2(1A) (a) to (c) have to be first complied with/fulfilled by the assessee. The Madras High Court in the case of *B. Nagi Reddi v. CIT* (2002) 258 ITR 719, following the judgment of Apex Court in the case of *Raja Benoy Kumar Sahas Roy* (1957) 32 ITR 466, has held, on identical facts, that the income derived for allowing a shooting of film in the agricultural land cannot be treated as agricultural income, as it has no nexus with the land, except that it was carried out on agricultural land.

Question 7

Explain in the context of provisions of the Act, whether the income derived during the year ended on 31.03.2012 in each of the following cases shall be subject to tax in the A.Y. 2012-13:

- (i) *Income of ₹ 75,000 derived by Anand Nursery from the sale of seedlings grown without carrying out all the basic operations on land.*
- (ii) *Mr. Gaitonde, born and brought up in the State of Sikkim, had a net profit of ₹ 2,25,000 from the business located in Sikkim and interest of ₹ 55,000 on the securities/bonds issued by the Government of Rajasthan.*
- (iii) *A political party, duly registered under section 29A of the Representation of the People Act, 1951, received rent of ₹ 1,25,000 per month of one of its building let out to a bank from 01.06.07.*

Answer

- (i) Explanation 3 to section 2(1A) provides that the income derived from saplings or seedlings grown in a nursery shall be deemed to be agricultural income, whether or not the basic operations were carried out on land. Accordingly, the income of ₹ 75,000 derived by Anand Nursery from the sale of seedlings grown without carrying out all the basic operations on land shall be treated as agricultural income and exempt from tax under section 10(1).
- (ii) Section 10(26AAA) exempts the income which accrues or arises to a Sikkimese individual from any source in the State of Sikkim and the income by way of dividend or interest on securities. Therefore, the income of Mr. Gaitonde from a business located in Sikkim and interest income on the securities/bonds of Government of Rajasthan shall not be subject to tax.
- (iii) Rent received by the political party from the bank is an income chargeable under the head "Income from house property". However, according to the provisions of section 13A, income from, *inter alia*, house property shall not be included in total income of a political party registered under section 29A of the Representation of the People Act, 1951, provided the political party fulfills the conditions as specified therein. Therefore, rent of ₹ 1,25,000 received by the registered political party from letting out of its building to a bank would not be included in its total income.

Question 8

What meaning has been assigned to "Venture Capital Undertaking" in section 10(23FB) of the Act?

Answer

Section 10(23FB) defines a venture capital undertaking to mean such domestic company whose shares are not listed in a recognised stock exchange in India and which is engaged in—

- (i) the business of -
 - (A) nanotechnology;
 - (B) information technology relating to hardware and software development;
 - (C) seed research and development;
 - (D) bio-technology;
 - (E) research and development of new chemical entities in the pharmaceutical sector;
 - (F) production of bio-fuels,
 - (G) building and operating composite hotel-cum-convention centre with seating capacity of more than three thousand; or
 - (H) developing or operating and maintaining or developing, operating and maintaining any infrastructure facility as defined in the Explanation to clause (i) of sub-section (4) of section 80-IA i.e.
 - (1) a road including toll road, a bridge or a rail system;
 - (2) a highway project including housing or other activities being an integral part of the highway project;
 - (3) a water supply project, water treatment system, irrigation project, sanitation and sewerage system or solid waste management system;
 - (4) a port, airport, inland waterway, inland port or navigational channel in the sea.
- (ii) dairy or poultry industry.

Therefore, exemption under this clause would be available only if the venture capital company/venture capital fund invests in the businesses or industries specified above. In such cases, tax would be payable by the investor under section 115U. If the venture capital company/venture capital fund invests in other businesses or industries, then it would not be eligible for exemption under this clause

Question 9

Ms. J, a Sikkimese woman, married Mr. K, a non-Sikkimese, on 1st January, 2008. During the previous year 2011-12, she received rent of ₹ 12 lacs from letting out of house properties

situated in the State of Sikkim. Is she liable to income-tax for assessment year 2012-13? Will your answer be different, if she had married Mr. K on 16th April, 2008?

Answer

Section 10(26AAA) provides that the following income, which accrues or arises to a Sikkimese individual, shall be exempt from income-tax:

- (1) Income from any source in the State of Sikkim; and
- (2) Income by way of dividend or interest on securities.

However, the aforesaid exemption will not be available to a Sikkimese woman, who marries a non-Sikkimese individual on or after 1st April, 2008.

Since Ms. J, the assessee, married Mr. K on 1st January, 2008, income derived by her by way of rent from properties situated in the State of Sikkim shall be exempt under section 10(26AAA).

However, if she had married Mr. K on 16th April, 2008, the exemption would not be available.

Note: The restriction in section 10(26AAA) applies only to Sikkimese women and not to men who are eligible for the exemption in respect of the above said incomes regardless of their marrying Sikkimese or non-Sikkimese women.

Question 10

State with reasons, based on the provisions of the Act, as to chargeability of the following receipts to tax in the assessment year 2012-13:

- (1) *Rent of ₹ 60,000 charged from tenants occupying houses constructed on the land situated in India and used for agricultural purposes.*
- (2) *Rameshwar Das Birla National award of ₹ 51,000 was given to Mr. X, a Chartered Accountant by "Rameshwar Dasji Birla Smarak Kosh" for his contributions and work.*
- (3) *Hundi superscribing "contributions in this hundi form part of corpus of trust fund" kept at Lord Venkateshwara Temple, Tirumala, was opened on 30.3.2012. Cash of ₹ 100 lacs and valuable articles worth ₹ 250 lacs were found to have been contributed by the devotees.*
- (4) *Minister of Surface Transport was in receipt besides salary an amount of ₹ 2,000 p.m. as entertainment allowance.*
- (5) *Rent of ₹ 30,000 for the period 1.4.2008 to 30.6.2009 due till the property sold out by the owner on 16.5.2011 was received on 12.2.2012 because of a court order.*

Answer

- (1) As per section 10(1), agricultural income is exempt from tax. The meaning and scope of agricultural income is defined in section 2(1A). According to *Explanation 2* to section 2(1A), any income derived from any building from the use of such building for any purpose (including letting for residential purposes or for the purpose of any business or

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profession) other than agriculture shall not be agricultural income. It appears in this case that the house was occupied for residential purposes. Therefore, the rent of ₹ 60,000 from letting out of houses constructed on agricultural land shall not be treated as agricultural income by virtue of *Explanation 2* to section 2(1A). Hence, such income would be chargeable to tax.

- (2) Section 10(17A)(i) exempts any payment made in pursuance of any award instituted in public interest by the Central Government or any State Government or instituted by any other body and approved by the Central Government in this behalf. As per *Notification No.199/19/98-IT(A-II) dated 15.11.2000*, the Rameshwar Das Birla National Award instituted by Rameshwar Dasji Birla Smarak Kosh was approved by the Central Government only for three assessment years viz. 1999-2000 to 2001-02. Hence, for A.Y.2012-13, no exemption would be available under section 10(17A).
- (3) As per section 11(1)(d), income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution shall not be included in the total income of the recipient. Therefore, in order to get the benefit under this section, it is necessary that the donor gives a specific direction that the voluntary contribution made by him should form part of the corpus of the trust. However, in this case, the donors have not given any specific directions that the contribution should form part of the corpus of the trust. Therefore, the benefit of exemption under section 11(1)(d) would not be available to the collections made through the hundi and such collections would be treated as income from the property held under trust.

It may be noted that the provision relating to taxability of anonymous donations @ 30% under section 115BBC does not apply to voluntary contributions received by a trust or institution created or established wholly for religious purposes.

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

- (4) The entertainment allowance received by the Minister of Surface Transport is taxable under the head "Salaries". However, deduction under section 16(ii) is allowable to the extent of least of the following –
- (i) 1/5th of the salary
 - (ii) ₹ 5,000
 - (iii) Actual entertainment allowance received, i.e., ₹ 24,000 in this case.

- (5) As per section 25AA, unrealised rent would be deemed to be the income chargeable under the head "Income from house property". Accordingly, it would be chargeable to income-tax as income of that previous year in which such rent is realised whether or not the assessee is the owner of that property in that previous year. Therefore, in this case, unrealised rent of ₹ 30,000 would be charged to tax in the P.Y.2011-12 under the head "Income from house property" even though he is no longer the owner of the house property.

Question 11

An amount of ₹ 5 lacs was paid on 17.3.2012 to the parents of Amit by the Government of Jharkhand as compensation to the aggrieved family, whose only son Amit lost his life in Maoist local bus bomb blast in Dantewada.

Explain with reasons, whether the amount of compensation received is chargeable to tax in A.Y. 2012-13?

Answer

Section 10(10BC) defines disaster to mean a catastrophe, mishap, calamity or grave occurrence in any area, arising from natural or man made causes, or by accident or negligence. It should have the effect of causing substantial loss of life or human suffering or damage to, and destruction of property, or damage to, or degradation of environment. It should be of such a nature or magnitude to be beyond the coping capacity of the community of the affected area.

If, for this reason, any compensation is paid by the Central Government or by a State Government or by a local authority, then the same will be exempt from tax. Accordingly, the amount of ₹ 5 Lacs received by the parents of deceased Amit from the Government of Jharkhand for the disaster because of Dantewada bus bomb blast it is exempt under section 10(10BC).

Question 12

Can an employee of a State Government claim exemption under section 10(10C) in respect of compensation received on voluntary retirement to the extent of ₹ 5 Lacs and relief under section 89(1) in respect of the amount of compensation in excess of ₹ 5 Lacs?

Answer

As per proviso to section 10(10C), where any relief was allowed under section 89 for any assessment year in respect of any amount received or receivable on voluntary retirement or termination of service or voluntary separation, no exemption under section 10(10C) shall be allowed in respect of the said sum in that assessment year or any other assessment year. Similarly, proviso to section 89 states that the relief under section 89 cannot be availed if benefit of exemption has been claimed u/s 10(10C).

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The employee of the State Government can, therefore, opt to claim exemption of ₹ 5 Lacs under section 10(10C) or relief under section 89(1) in respect of compensation received on voluntary retirement, but not both.

Question 13

R purchased equity shares in P Ltd., a constituent of BSE-500 index on Mumbai Stock Exchange on 1st March, 2009. He sold the shares on 4th March, 2012 at a loss of ₹ 10,000. He wants to set off the loss against other long-term capital gain during the year. Examine whether such set off is permissible. Both purchase and sale transactions were entered into on a recognized stock exchange.

Answer

Section 10(38) exempts long term capital gain arising from transfer of equity shares in a company or a unit of an equity oriented fund, if such transfer has been subjected to Securities Transaction Tax. Hence, the capital gain / capital loss will have no tax implication.

In this case, the assessee has suffered a loss of ₹ 10,000 by selling eligible equity shares. It is settled principle the loss arising from an exempt source, is not eligible for set off against income arising from a taxable source. In the case of *JCIT Vs. Thyagarajan.S.S (1981) 129 ITR 115 (Mad)*, the Madras High Court held that loss incurred by an assessee from an exempted source, cannot go to set off income from a taxable source. In view of the same, the set off in the instant case is not permissible.

Question 14

A Public Sector Company has engaged you to frame a scheme of voluntary separation for its employees so that the amount received by the employees under the scheme would qualify for tax exemption under section 10(10C). What points would you bear in mind while drawing up the scheme? What will be the tax treatment of the payments under the scheme in the hands of the company?

Answer

Section 10(10C) provides that any amount received or receivable by an employee of a public sector company at the time of his voluntary retirement or termination of service under a scheme of voluntary separation is exempt to the extent such amount does not exceed ₹ 5,00,000. The scheme, however, should be framed in accordance with the guidelines prescribed under Rule 2BA.

The guidelines in Rule 2BA provide that the scheme of voluntary separation framed by a public sector company should be in accordance with the following requirements in order to be eligible for exemption –

- (i) The scheme will apply to an employee who has completed 10 years of service or completed 40 years of age.

- (ii) The scheme should apply to all employees (by whatever name called) including workers and executives of the company except directors.
- (iii) The scheme should result in overall reduction in the existing strength of the employees of the company.
- (iv) The vacancies caused by voluntary separation, should not be filled up.
- (v) The retiring employee should not be employed in another company or concern belonging to the same management.
- (vi) The amount receivable on voluntary separation should not exceed the amount equivalent to three months salary for each completed year of service or salary at the time of retirement multiplied by the balance of months' of service left before the date of retirement on superannuation.

Section 35DDA provides that, in the case of the company, where any expenditure has been incurred by way of payment to an employee under the scheme of voluntary retirement, one-fifth of the amount so paid shall be deducted in computing the profits and gains of the business for that previous year and the balance shall be deductible in equal installments in each of the four immediately succeeding previous years.

Note: It may be noted that if exemption under section 10(10C) in respect of VRS compensation is opted by the taxpayer, he is not eligible for further relief under section 89 of the Act.

Question 15

Amit, a captain in Indian army, was killed at Kashmir border during a war. The widow of Amit was paid an ex-gratia payment of ₹ 5,00,000 in March, 2012, besides the family pension during the year of ₹ 2,40,000. She wants to know the taxability of both the receipts. Decide.

Answer

According to CBDT Circular No.776 of June 8, 1999, any lumpsum ex-gratia payment made by the Central Government / State Government/Local Authority or Government, public sector undertaking, to the widow or other legal heirs of an employee, who dies while in active service, will not be taxable as income under the Income-tax Act, 1961. Therefore, ₹ 5,00,000 is not taxable.

Section 10(19) grants tax exemption in respect of family pension if a member of the armed forces dies in the course of operational duties. Hence, if captain Amit had died in the course of operational duties, the family pension received by widow of captain Amit is fully exempt from tax.

Question 16

Does the tax borne by employer on behalf of employee in respect of provision of non-monetary perquisites constitute an income in the hands of employee? What are the tax implications of such payment in the hands of employer?

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Answer

Section 10(10CC) provides that in the case of an employee deriving income in the nature of non-monetary perquisites, the amount of tax on such income paid by the employer, is exempt from tax in the hands of the employee. In view of this, by virtue of exemption provided in section 10(10CC), the tax borne by the employer on behalf of employees in respect of provision of non-monetary perquisites is exempt in the hands of the employee.

As regards tax implications of such payment in the hands of employer section 40(a)(v) provides for disallowance of the tax actually paid by employer under section 10(10CC) while computing the income chargeable under the head "Profit and gains of business or profession".

Question 17

"Save Wild Life" an institution having its main object as 'preservation of wildlife', used the entire income derived from an activity in the nature of trade for its main object during the previous year ended on 31.03.2012. The institution seeks your opinion to know whether such utilization of its income be treated for "charitable purpose"? Would your answer be different, if the main object of the institution is "advancement of object of general public utility"?

Answer

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

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

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

It may be noted that if the receipts from such activity does not exceed ₹ 25 lacs in that year, then, the institution would not lose its "charitable" status, even its main object is "advancement of any other object of general public utility".

Question 18

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

Answer

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

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

Question 19

"Capital expenditure cannot be said to be application of income by a trust under section 11(1)(a) of the Income-tax Act, 1961." Examine the validity of this statement

Answer

This statement is not valid, since, if the income is applied for the purchase of a capital asset for the purposes of the trust, it would still constitute application of income for charitable purpose. If an assessee invests in construction of a building so as to augment its resources for fulfilling the objectives of the institution, the same would be considered as application for charitable purpose. Similarly, repayment of loan taken for construction of a building or construction of a commercial complex so as to augment the resources of the trust would also amount to application of income for charitable purposes.

Question 20

Asha Memorial Trust running hospitals is registered under section 12A. Following particulars relevant for the previous year ended 31st March, 2012 are furnished to enable you to compute tax liability of the trust.

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- (i) Income from running of hospitals ₹ 14.25 lacs.
- (ii) Donation received (including anonymous donation ₹ 3 lacs) ₹ 5.75 lacs.
- (iii) Amount applied for the purposes of hospital ₹ 13 lacs.
- (iv) The trust had accumulated ₹ 15 lacs under section 11(2) in the financial year 2005-06 for a period of five years for extension of one of its hospitals. The trust has spent ₹ 13.50 lacs for the said purpose till 31st March, 2011.

Compute the taxable income of the trust and tax payable by Asha Memorial Trust for the assessment year 2012-13.

Answer

Computation of taxable income of Asha Memorial Trust for A.Y. 2012-13

Particulars	Amount in ₹	
Income from running of hospitals	14,25,000	
Donation other than anonymous donation	<u>2,75,000</u>	17,00,000
Less: 15% of income of ₹ 17 lacs accumulated or set apart under section 11(1)(a)	2,55,000	
Amount applied for the purposes of hospital	<u>13,00,000</u>	<u>15,55,000</u>
		1,45,000
Add: Amount accumulated for extension of a hospital but not spent deemed to be income under section 11(3) (₹ 15 lacs – ₹ 13.50 lacs) (See Note 1 below)		<u>1,50,000</u>
		2,95,000
Add: Anonymous donation taxable @30% under section 115BBC (See Note 2 below)		<u>3,00,000</u>
Total Income		<u>5,95,000</u>
Tax on above:		
Tax on anonymous donation of ₹ 2 lacs at 30% (See Note 2 below)		60,000
Tax on other income of ₹ 2,95,000 at normal rates		
Upto ₹ 1,80,000	Nil	
Over ₹ 1,80,000 up to ₹ 2,95,000 @ 10%	<u>11,500</u>	<u>11,500</u>
		71,500
Education cess @2%		1,430
Secondary and higher education cess@1%		<u>715</u>
Tax payable		<u>73,645</u>

Notes:

- (1) Section 11(3) provides that if the income accumulated for certain purpose is not utilized for the said purpose within the period (not exceeding 5 years) for which it was accumulated, or in the year immediately following the expiry thereof, then the unutilised amount is deemed to be the income of the charitable institution for the previous year immediately following the expiry of the period of accumulation. In the instant case, Asha Memorial Trust accumulated ₹ 15,00,000 in the previous year 2005-06 for extension of one of its hospitals for a period of 5 years. Period of accumulation thus expired on 31.3.2011. The assessee has spent ₹ 13,50,000 out of accumulated sum of ₹ 15,00,000 up to 31.3.2011. Therefore, the unutilised amount of ₹ 1,50,000 is deemed to be income of the previous year 2011-12 (A.Y. 2012-13). It is assumed that the amount of ₹ 1,50,000 was not utilized during the P.Y.2011-12 also.
- (2) Only the anonymous donations in excess of the exemption limit specified below would be subject to tax@30% under section 115BBC.

The exemption limit is the higher of the following –

- (1) 5% of the total donations received by the assessee [i.e., ₹ 28,750 (5% x 5.75 lacs)]; or
- (2) ₹ 1 lacs.

Therefore, in this case the exemption would be ₹ 1 lacs.

The total tax payable by such institution would be –

- (1) tax@30% on the anonymous donations exceeding the exemption limit as calculated above [i.e., tax@30% on ₹ 2,00,000, being ₹ 3,00,000 – ₹ 1,00,000]; and
- (2) tax on the balance income i.e., total income as reduced by the aggregate of anonymous donations received.

Question 21

A public charitable trust, created under a trust deed for providing relief to disabled persons, registered under section 12A, furnishes the following particulars of its receipts during the year ended 31st March, 2012 -

		₹ (in Lacs)
(i)	Income from properties held by trust (net)	20
(ii)	Income (net) from business (incidental to main objects)	17
(iii)	Voluntary contributions from public (including the corpus donation of ₹ 5 Lacs)	11

The trust applied ₹ 20 Lacs towards various activities and programmes undertaken for the benefit of autistic persons during the year. The trust has also paid ₹ 10 Lacs towards

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repayment of a loan taken a year back for the purpose of construction of its centre for training the disabled persons in various handicraft works.

Determine the tax liability, if any, of the trust for the assessment year 2012-13.

Answer

Computation of total income of the trust for the A.Y. 2012-13

Particulars	₹	₹
Income from properties held by trust	20,00,000	
Income from business incidental to the main objects of the trust	17,00,000	
Voluntary Contribution other than corpus donation (Note 1)	6,00,000	43,00,000
Less: 15% of income accumulated or set apart under section 11(1)(a)		6,45,000
		36,55,000
Less: Amount applied for charitable purposes		
Activities and programmes for the benefit of autistic persons	20,00,000	
Repayment of loan taken for construction of training centre (Note 2)	10,00,000	30,00,000
Taxable Income		6,55,000

Computation of tax liability of the trust for the A.Y. 2012-13

Particulars	₹	₹
Upto ₹ 1,80,000	Nil	
₹ 1,80,000 – ₹ 5,00,000	32,000	
₹ 5,00,000 – ₹ 6,55,000	31,000	63,000
Add: Education cess @ 2%		1,260
Add: Secondary and higher education cess @ 1%		630
Total tax liability		64,890

Notes:

- (1) Section 11(1)(d) excludes from the total income of the person, any income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution.
- (2) In *CIT vs. Janmabhumi Press Trust (2000) 242 ITR 703*, the Karnataka High Court held that where a debt is incurred for the purpose of the trust, the repayment of the debt would amount to an application of the income for the purpose of the trust. Therefore,

repayment of loan taken for construction of training centre for disabled persons is to be considered as application for charitable purpose.

Question 22

An institution operating for promotion of education claiming exemption under section 11 since 1993 furnishes the following data for the assessment year 2012-13.

Sl. No.	Particulars	₹ in crores
(i)	Fees collected from students	14
(ii)	Expenses incurred to run the institution	4
(iii)	Land acquired to be used as a cricket field for the students	2
(iv)	Amount earmarked and set apart for construction of an arts block within the next 4 years.	4

Compute the total income of the institution for the A.Y.2012-13.

Answer

Computation of total income of the institution for the A.Y. 2012-13

Particulars	₹ in crores
Fees received	14.00
Less : Expenses incurred to earn the income	<u>4.00</u>
	10.00
Less : 15% (exempt even if not spent for the objects of the institution)	<u>1.50</u>
	8.50
Less : Accumulated for specified purpose (See Note 1)	<u>4.00</u>
Balance to be spent	4.50
Actual amount spent on purchase of land for cricket field (See Note 2)	<u>2.00</u>
Total income	<u>2.50</u>

Notes –

- Section 11(2) provides that a trust/institution can accumulate or set apart its income for a specified purpose by informing the concerned Assessing Officer. However, the period for which the funds can be accumulated cannot exceed 5 years. The amount so accumulated should be invested in the specified forms and modes. In this case, the institution has to inform the concerned Assessing Officer and invest ₹ 4 crore in the specified forms and modes.
- The institution must utilise 85% of its income within the previous year for the objects of the institution. The institution can apply its income either for revenue expenditure or for capital expenditure provided the expenditure is incurred for promoting the objects of the institution. Land acquired and meant for use as cricket field for students is a capital

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expenditure incurred for promoting the objects of the institution and hence eligible for deduction.

Question 23

A charitable trust derives its income from the business of providing mineral water to various companies situated in software technology park in Hyderabad. A sum of ₹ 30 lacs has been derived as net income from such business activity, which has been applied for the object of general public utility. Examine the taxability of application of the income, if the income so derived relates to the previous year 2011-12. Would your answer be different, if the trust runs a school in a backward district and applies the profits from the business for such school's activity?

Answer

Section 2(15) defines "charitable purpose" to include relief of the poor, education, medical relief, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest and the advancement of any other object of general public utility. However, "advancement of any other object of general public utility" would 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 of any service in relation to any trade, commerce or business, for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity or the retention of such income, by the concerned entity.

"Advancement of any other object of general public utility" would continue to be a "charitable purpose", if the total receipt from any activity in the nature of trade, commerce or business, or any activity of rendering any service relation to any trade, commerce or business does not exceed ₹ 25 lacs in the previous year.

Therefore, in the first case, net income from the business of supplying mineral water to various companies i.e. ₹ 30 lacs is not eligible for exemption under section 11 since the receipt from such activity exceeds ₹ 25 lacs during the year. This is because "advancement of any object of general public utility" would not be a charitable purpose if it involves carrying on of any activity in the nature of trade, commerce or business, for example, supply of mineral water for a consideration, as in this case. It is immaterial that the net income from such business is applied for the object of general public utility.

On the other hand, where the trust runs a school in a backward district, this restriction is not applicable. The reason is that the restriction contained in section 2(15) is applicable only to the fourth limb of the definition of "charitable purpose" i.e. advancement of object of general public utility. It does not affect the other three limbs of the definition viz. "relief of the poor", "education", and "medical relief".

Section 11(4) clarifies that "property held under trust" includes a business undertaking so held. As per section 11(4A), exemption can be availed in respect of profits and gains of business, if such business is incidental to the attainment of the objectives of the trust and separate books

of account are maintained in respect of such business. Therefore, in the second case, the profit from the business shall be eligible for exemption under section 11, assuming that the said business is incidental to the attainment of the objects of the trust (i.e., education) and books of account for such business activity is maintained separately.

Question 24

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

- (i) *Rural reconstruction and upliftment of the masses through Cottage Industry.*
- (ii) *Welfare of industrial workers with a stipulation that the workers of settlor of trust have got preference over others.*

Answer

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

"Advancement of any other object of general public utility" would continue to be a "charitable purpose", if the total receipt from any activity in the nature of trade, commerce or business, or any activity of rendering any service relation to any trade, commerce or business does not exceed ₹ 25 lacs in the previous year.

- (i) The Supreme Court has, in *Thiagarajar Charities vs. Addl. CIT (1997) 225 ITR 1010*, observed that "cottage industry" is associated with the idea of a small, simple enterprise or industry in which employees work in their own houses or in a small place, gathered together for the purpose, using their own equipments and is usually found in rural areas or so carried on, by the poorer section of the society. In substance, the activity of rural reconstruction and upliftment of masses through cottage industry is to afford relief to the poor and consequently, it is for charitable purpose.
- (ii) The welfare of industrial workers with a stipulation that the workers of settlor of trust have preference over others would also constitute "charitable purpose" within the meaning of section 2(15). The Patna High Court has, in *CIT v. Tata Steel Charitable Trust (1993) 203 ITR 764*, observed that exemption under section 11(1) can be availed only if the following conditions are satisfied –
 - (1) the trust is created for a charitable purpose; and

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- (2) no part of the income of such trust enures or has been used or applied directly or indirectly for the benefit of any person referred to in section 13(3).

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

Question 25

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

	Amount (₹)
Cost of transferred asset	2,40,000
Sale consideration	3,60,000
Cost of new asset purchased	3,00,000

Answer

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

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

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

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

Question 26

Can a trust created for charitable purposes in February 2011, having filed application for registration as per section 12A on 11.4.2011, claim benefits of sections 11 and 12 from Assessment Year 2011-12?

Answer

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

Therefore, since the trust has filed application for registration only on 11.4.2011, it cannot claim benefits of section 11 and 12 from A.Y. 2011-12. The exemption would be available only from the A.Y. 2012-13 relevant to the P.Y. 2011-12.

Question 27

Bharat Charitable Trust created on 1.1.2010 applied for registration of trust under section 12A of the Income-tax Act before the Commissioner of Income-tax on 1.7.2011 and requested for condonation of delay.

- (i) *Explain with reasons the period for which the trust is eligible to get exemption under section 11 and 12 of the Income-tax Act, 1961.*
- (ii) *Can the exemption under sections 11 and 12 for A.Y. 2011-12 be denied if the trust is holding investments in equity shares of a public sector company since 01.07.2011?*
- (iii) *The Trust has also applied for granting exemption under section 80G of the Income-tax Act, 1961. But the approval for the same has been rejected by the Commissioner of Income-tax under section 80G(5)(vi) of the Income-tax Act on 30.9.2011. The Trust seeks your advice on whether it can file an appeal against the said rejection before the higher authorities.*

Answer

- (i) As per section 12A(2), in respect of applications filed on or after 1st June, 2007, the provisions of section 11 and 12 shall apply in relation to the income of the trust from the assessment year relevant to the financial year in which the application is made i.e. the exemption would be available only with effect from the assessment year relevant to the previous year in which the application is filed. It would not be available in respect of any earlier assessment year. Further, the power of the Commissioner to grant registration for past years, by condoning the delay in filing such application, has also been removed. Hence, Bharat Charitable Trust shall be eligible to get exemption under section 11 and 12 with effect from the financial year in which the application is made i.e. assessment year 2012-13 onwards.
- (ii) A trust registered under section 12A cannot be denied exemption for holding shares in a public sector company in view of section 13(1)(d)(iii). Hence, the exemption under section 11 and 12 cannot be denied to the trust for holding investments in equity shares of a public sector company.

- (iii) Section 253 provides that an appeal can be filed before the Appellate Tribunal against an order passed by the Commissioner under section 80G(5)(vi) rejecting the application of such trusts for the purpose of recognition under section 80G.

Question 28

The following trusts claim that anonymous donations received by them during the financial year 2011-12 are not liable to tax under section 115BBC:

- (i) *A charitable trust referred to in section 11 which applied the entire amount of anonymous donations for purposes of the trust during the relevant financial year.*
- (ii) *A trust established wholly for religious purposes which applied 75% of the amount of anonymous donations for the purposes of the objects of the trust during the relevant financial year.*

Examine the validity of the claim made by the trusts.

Answer

- (i) Section 115BBC(1) provides for levy of tax @ 30% on anonymous donation received by, *inter alia*, charitable trusts or institutions referred to in section 11. Further, section 13(7) provides that the exemption provisions contained in sections 11 and 12 shall not be applicable in respect of any anonymous donation liable to tax under section 115BBC. As such, application of the anonymous donations received by the charitable trust for charitable purposes does not confer any exemption from tax. Therefore, the claim for non-taxability under section 115BBC of anonymous donations received by the charitable trust is not valid in law.

However, anonymous donation would be exempt upto the higher of –

- (1) ₹ 1 Lac
- (2) 5% of total donations received by the assessee
- (ii) Section 115BBC(2) provides that the provisions contained in section 115BBC(1) relating to the taxability of anonymous donations are not applicable to any trust or institution created or established wholly for religious purposes. As such, the trust established wholly for religious purposes is not liable to be taxed in respect of the anonymous donations received by it. The application or non-application of such anonymous donation for the purposes of trust during the relevant financial year is not germane to the issue of taxability under section 115BBC.

Question 29

A charitable trust registered under section 12AA of the Income-tax Act, 1961 has, out of its income of ₹ 3,90,000 for the year ending 31.3.2012 and sale proceeds of a capital asset, held by it for less than 36 months, amounting to ₹ 9,60,000, purchased a building during the year ending 31.3.2012 for ₹ 13,50,000. The capital asset was sold during the year ending 31.3.2012. The building is held only for charitable purposes. The trust claims that the

purchase of the building amounts to application of its income for charitable purposes and that the capital gain arising on the sale of the capital asset is deemed to have been applied to charitable purposes. Is the claim made by the charitable trust valid in law?

Answer

Section 11(1)(a) stipulates that in order to avail exemption of income derived from property held under trust wholly for charitable or religious purposes, the trust is required to apply for charitable or religious purposes, 85% of its income from such property. In this case, the trust has earned income of ₹ 3,90,000 for the year ended 31.3.2012. It has also earned short term capital gain from sale of capital asset for ₹ 9,60,000. The trust had utilized the entire amount of ₹ 13,50,000 for the purchase of a building meant for charitable purposes.

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

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

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

Question 30

A charitable trust, whose income can be exempt under section 11 of the Income-tax Act, 1961, was formed on 1st March, 2007. For the accounting year ended 31st March, 2012, it earned an income of ₹ 3,60,000.

It filed with the Commissioner of Income-tax its application for registration on 30th March, 2011 explaining that for good and sufficient reasons, it was prevented from filing the application by the due date.

State:

- (i) *by which date the application for registration should have been filed;*
- (ii) *whether such an application could have been filed before the formation of the trust;*
- (iii) *in the absence of an order of registration from the Commissioner, can the trust be deemed to be registered;*
- (iv) *the steps to be taken by the trust to secure exemption from income-tax;*
- (v) *whether a certificate of registration once granted can be cancelled and if so, the conditions there for.*

Answer

- (i) The requirement of filing an application for registration under section 12A within one year of creation of the trust has been removed. The application can be filed at any time now. Accordingly, the provisions of sections 11 and 12 would apply from the assessment year relevant to the financial year in which the application is made i.e. the exemption would be available only with effect from the assessment year relevant to the previous year in which the application was filed. It would not be available in respect of any earlier assessment year.
- (ii) No. The application for registration u/s 12A cannot be filed before the formation of the trust.
- (iii) As per section 12AA(2), every order granting or refusing registration should be passed before the expiry of 6 months from the end of the month in which the application was received under section 12A. The Act does not provide for deeming registration of a trust in the absence of an order of registration from the Commissioner.
- (iv) The following are the steps to be taken by the trust to secure exemption from income-tax:
 - (1) The trust should be registered with the Commissioner of Income-tax under section 12A.
 - (2) The accounts of the trust for the previous year must be audited by a Chartered Accountant if its total income without giving effect to the provisions of section 11 and section 12 exceeds the maximum amount which is not chargeable to tax. The audit report in the prescribed form, duly signed and verified by the Chartered Accountant, should be furnished along with the return of income of the trust for the relevant assessment year.
 - (3) At least 85% of the income is required to be applied for the approved purposes.
 - (4) The unapplied income and the money accumulated or set apart should be invested or deposited in the specified forms or modes.
- (v) Yes, the certificate of registration can be cancelled by the Commissioner. According to section 12AA, if the Commissioner is satisfied that the activities of the trust are not genuine or are not being carried out in accordance with the objects of the trust, he shall, after giving the trust a reasonable opportunity of being heard, pass an order in writing canceling the registration of the trust.

Question 31

Gangaram Public Charitable Trust runs a hospital, which derived income of ₹ 250 Lacs, from its operational activities. Expenses incurred to earn such income are ₹ 55 Lacs. Depreciation on various assets used in the hospital is ₹ 15 Lacs. Out of income of ₹ 250 Lacs, the amount accrued but not received as on 31-03-2012 is ₹ 20 Lacs. The institution earmarked and set apart ₹ 30 Lacs in March, 2012 to give as advance for a building intended to be taken on lease for expansion of the hospital, but the amount was paid on 7th April, 2012, as the lease

agreement could not be signed by 31st March, 2012. The trust has got an ERP package developed and installed by an IT company during the year. The total cost to the trust on account of the ERP package was ₹ 85 Lacs. Advice the trust on its total income, if the trust has incurred ₹ 12 Lacs for purchase of a number of desktop and laptop computers for use in the hospital.

Answer

The total income of the trust for the A.Y. 2012-13 is computed hereunder:

Particulars		₹ (in Lacs)	
Income derived from property held under trust			250
Less:	Expenses incurred thereto	55	
	Depreciation on assets	15	70
			180
Less:	15% eligible for blanket exemption without any conditions (15% of ₹ 180 Lacs)		27
			153
Less:	Income not received during the year, which can be spent in the year of receipt or in the immediately following year		20
			133
Less:	Non-application of income due to delay in signing lease agreement [The amount was applied on 7 th April in the immediately following year – Option to be exercised in writing before the expiry of the time allowed under section 139(1) for furnishing the return of income]		30
Amount to be applied for the objects of the trust by 31.3.2012			103
Less:	Amount applied for the objects of the trust		
	(i) For development and installation of ERP package for the purpose of the trust	85	
	(ii) For purchase of desktop and laptop computers for the purposes of the trust	12	97
Taxable Income			6

Note -

- (i) Depreciation should be allowed while computing income of a trust under section 11(1)(a). A trust can claim depreciation on assets even if the cost of assets has been fully allowed as application of income under section 11 in the past years. Even when the whole of capital expenditure has been treated as an application of income for charitable purpose u/s 11, the trust can still claim depreciation on assets used for its purposes on the basis of normal commercial principles.

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- (ii) If the income applied to charitable purposes in India falls short of 85% of the income derived during the year from property held under trust for the reason that the whole or any part of its income has not been received during that year, then such income, at the option of the person in receipt of income, can be applied during the previous year in which the income is received or in the immediately following previous year. The option is to be exercised in writing before expiry of the time allowed u/s 139(1) for filing return of income.
- (iii) The word "applied" used in section 11 means that the income is actually applied for the charitable purposes of the trust. The word "applied" does not necessarily imply "spent". Even if a certain amount is irretrievably earmarked and allocated for charitable purposes, the said amount can be deemed to have been applied for charitable purposes. [*CIT vs. Trustees of H.E.H. Nizams Charitable Trust, (1981) 131 ITR 497 (AP).*]
- (iv) The cost of getting an ERP package developed and installed is a capital expenditure. A charitable trust can apply its income either for revenue expenditure or for capital expenditure provided the expenditure is incurred for promoting the objects of the trust. Purchase of a fixed asset to be utilised for the purpose of the trust amounts to application of income for charitable purposes as held by the Supreme Court in *S.R.M.C.T.M.Tiruppani Trust vs. CIT (1998) 230 ITR 636*.

Question 32

A public charitable trust registered under Section 12A, for the previous year ending 31.3.2012, derived gross income of ₹16 Lacs, which consists of the following: (₹ in Lacs)

- (a) Income from properties held by trust (net) 5
- (b) Income (net) from business (incidental to main objects) 4
- (c) Voluntary contributions from public 7

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

Determine the taxable income of the trust for the assessment year 2012-13.

Answer

(i) Statement of computation of income of public charitable trust

(i)	Income from property held under trust (net)	5,00,000
(ii)	Income (net) from business (incidental to main objects)	4,00,000
(iii)	Voluntary contributions from public	7,00,000
	Voluntary contribution made with a specific direction towards corpus are alone to be excluded under section 11(1)(d). In this case, there is no such direction and hence, included.	--
		16,00,000

Less: 15% of the income eligible for retention / accumulation without any conditions		2,40,000
		13,60,000
Deduct: Amount applied for the objects of the trust		
(i)	Amount spent for charitable purposes (₹ 11,60,000 - 3,60,000)	8,00,000
(ii)	Repayment of loan for construction of orphan home	<u>3,60,000</u>
		11,60,000
Taxable Income		2,00,000

Note : The trust may opt for accumulation of income by giving a notice in writing to the Assessing Officer in the prescribed form along with the return of income or before the completion of assessment and such accumulation to the extent of ₹ 2 Lacs would save the trust from tax burden.

Question 33

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

Ramji Charitable Trust has filed return of income for the Assessment Year 2012-13 within the stipulated time under section 139(1) and applied only 50% of its income to specified purposes. It intends to accumulate the balance 25% of income to be spent in future years. While completing the assessment, the Assessing Officer disallowed the accumulated income of 25% and taxed the same on the ground that the trust has not made any application under Section 11(2) along with return of income or even before the completion of assessment. Discuss the validity of the action of the Assessing Officer in this case.

Answer

Section 11(2) provides that a charitable trust has to apply 85% of its income to charitable or religious purposes and where 85% of its income is not applied in the aforesaid manner, the trust may accumulate or set apart either the whole or part of its income for future application for such purposes in India. The requirement of the Act is that the trust has to make an application/intimation in the prescribed form for accumulation of income which should be filed or furnished before the assessing authority along with the return of income under section 139(1).

This requirement of filing application is mandatory and without those particulars, the assessing authority cannot entertain the claim of the assessee under section 11. Further, any claim for giving benefit of section 11 on the basis of information supplied subsequent to the completion of assessment would mean that the assessment order will have to be reopened. The Act does not contemplate such reopening of the assessment. Hence, furnishing of application for accumulation after completion of assessment cannot be accepted. This principle is settled in

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CIT vs. Nagpur Hotel Owners Association 247 ITR 201 (SC). Therefore, the action of the Assessing Officer is correct.

Question 34

A trust set up wholly for charitable purposes furnishes its return of income in respect of assessment year 2011-12 on 15.11.2011, declaring an income of ₹ 2 Lacs. The Assessing Officer on scrutiny of the return finds that the income of the trust is exempt from tax. Are there any penal consequences for the trust's failure to furnish the return of income within the prescribed time?

Answer

As per section 139(4A), every person in receipt of income derived from property held under trust or other obligation wholly for charitable or religious purposes or in part only for such purposes or of income being voluntary contributions referred to in section 2(24)(ia) shall if the total income (without giving effect to the provisions of section 11 and 12) exceeds the maximum amount which is not chargeable to tax must furnish return of income in the prescribed form and in the prescribed manner.

Since the income of the trust has been found to be exempt under section 11 and 12, no interest under section 234A for delay can be charged.

However, under clause (e) of sub-section (2) of section 272A, the person who is required to file a return in his representative capacity will be liable to pay by way of penalty a sum which shall not be less than ₹ 100 for every day during which the failure continues.

Such a penalty can be levied by the Joint Commissioner and a reasonable opportunity of hearing has to be given [sub-section (3) of section 272A]. Further, under section 273B, no penalty is leviable under section 272A, if the person proves that there was reasonable cause for the said failure.

Question 35

Ramamurty Public Charitable Trust (Registered under section 12A of the Income-tax Act, 1961) furnishes the following data for the financial year ending 31.3.2012.

		(₹ in Lacs)
(i)	Income from Engineering College (Gross receipts ₹ 100 Lacs)	10
(ii)	Income from properties held in trust (out of his ₹ 2 Lacs was not received during the year and ₹ 2 Lacs was received only on the last day of the year)	26
(iii)	Net income from business held under trust (As incidental to the main objects) as per books	2
(iv)	Amount spent on free scholarship, free meals and free medical relief	9
(v)	Repayment of loan taken for construction of Health Care Centre	3

You are required to:

- (a) Compute the taxable income of the Trust for the assessment year, 2012-13. Assume that option is exercised under explanation to section 11(1) of the Act.
- (b) Advise how the taxability on the computed income could be minimized or reduced.

Answer

- (a) Computation of total income of Shri Ramamurthy Public Charitable Trust for A.Y. 2012-13**

		(₹ in Lacs)
(i)	Income from Engineering College – exempt under section 10(23C)(iiiad) as gross receipts do not exceed ₹ 1 crore.	Nil
(ii)	Income from properties held under trust	26.00
(iii)	Income from business undertaking held under trust (assumed that the business is incidental to the attainment of objectives of the trust and separate books are maintained satisfying section 11(4A))	2.00
		28.00
	85% of the income required to be spent (85% of ₹ 28 Lacs)	23.80
	Less : Amount spent on free scholarship, free meals and free medical centre	(-)9.00
	Repayment of loans for construction of health centre (this is utilized for the fulfillment of the objects of the trust) See <i>CIT v. Janmbhoomi Press Trust</i> 242 ITR 703)	(-)3.00
		11.80
	Less: Option exercised under explanation 2 to section 11 of the Act	
	(i) Amount not received during the previous year	2.00
	(ii) income received on the last day to be spent in the next year	2.00
	Income of the trust liable to tax	7.80

- (b) In order to minimize and /or reduce the tax liability, the trustees may give a notice in writing to the Assessing Officer in the prescribed manner about their intention to accumulate the unspent amount of ₹ 7.80 Lacs specifying the period and the purpose for which, the accumulation is proposed to be made and invest the sum of ₹ 7.80 Lacs in specified assets as per section 11(5). This accumulation would be in compliance with section 11(2) and in such case no tax will be payable on the sum of ₹ 7.80 Lacs.

Question 36

The books of account maintained by a National Political Party registered with Election Commission for the year ended on 31.3.2012 disclose the following receipts:

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(a)	Rent of property let out to a departmental store at Chennai	₹ 6,00,000
(b)	Interest on deposits other than banks	₹ 5,00,000
(c)	Contributions from 100 persons (who have secreted their names) of ₹ 11,000 each	₹ 11,00,000
(d)	Contribution @ ₹ 11 each from 1,00,000 members in cash	₹ 11,00,000
(e)	Net profit of cafeteria run in the premises at Delhi	₹ 3,00,000

Compute the total income of the political party for the year 2012-13, with reasons for inclusion or otherwise.

Answer

The total income of a political party registered with the Election Commission is to be computed as per section 13A under which the income derived from house property, income from other sources and income by way of voluntary contributions received from any person on fulfilling of the conditions as mentioned thereunder are exempt from tax.

Computation of income of National Party

	Particulars	Amount
(a)	The rent of the property of ₹ 6 Lacs located at Chennai	Nil
(b)	The interest received on deposits of ₹ 5 Lacs	Nil
(c)	The contributions given by 100 persons of ₹ 11,000 each by secreting their identities (see note below)	Nil
(d)	The contribution of ₹ 11 each given by its members being recorded in the books	Nil
(e)	Net profit of cafeteria at Delhi	3,00,000
	Total Income	3,00,000

Note:

In respect of each voluntary contribution in excess of ₹ 20,000, exemption would be available only if the political party keeps and maintains a record of such contribution and the name and address of the person who has made such contribution. However, in this case, this provision is not attracted since the contribution given by each person is less than ₹ 20,000.

Self-examination questions

1. The Income-tax Act, 1961 grants exemption from tax to political parties in respect of their income. State the incomes so exempted as per the provisions of the Act.
2. Explain the meaning of the following terms in the context of section 10AA -
 - (a) Export;
 - (b) Export turnover;
 - (c) Manufacture.
3. (a) Discuss the exemption available under the Income-tax Act in respect of specified

income arising from any international sporting event in India.

- (b) What are the exemptions available under section 10 in respect of companies engaged in the business of generation or transmission or distribution of power and subsidiaries of such companies? What are the conditions to be fulfilled to avail such exemptions?
4. Explain about aggregation of agricultural income for rate purposes. How will income-tax be computed where an individual derives agricultural as well as non-agricultural income?
 5. Discuss the provisions of section 10AA in respect of tax holiday for newly established units in a special economic zone.
 6. When can a charitable trust avail benefits under section 11 & 12 of the Income-tax Act, 1961?
 7. Discuss the meaning and tax treatment of anonymous donations received by charitable/religious trusts/institutions.
 8. Mr. Ganesh, an employee of a co-operative bank, received a certain sum by way of leave encashment while in service from his employer, in respect of which he claimed exemption under section 10(10AA), on the contention that the words 'or otherwise' in section 10(10AA) clearly indicated that the exemption was to be given as and when there was a payment to the assessee in lieu of leave encashment and the words 'or otherwise' therein did not restrict the purview of the exemption to retiring employees only. Is Mr. Ganesh correct in claiming exemption under section 10(10AA) in respect of leave encashment received by him while in service? Discuss.

Answer

8. This issue came up before the *Allahabad High Court in CIT v. Vijai Pal Singh (2005) 144 Taxman 504*. The High Court observed that the words 'or otherwise' would draw the restricted meaning *qua* the immediately preceding word 'superannuation'. The superannuation is of an employee's severance of relationship of contract of employment with the employer. The phrase 'or otherwise' would cover only such an eventuality when there is severance of relationship of employer and employee and contract of employment. Therefore, the phrase 'or otherwise' will not cover such cases where there is no severance of relationship of employer and employee and the assessee continues to be under the employment of the same employer, and receives leave encashment. The Court held that this interpretation is in consonance with the legislative history of the section and it manifests the intention of the Legislature to give a limited benefit to an employee with respect to the income received by the employee at the time of his retirement or superannuation or severance of relationship.

Therefore, in view of the above case, exemption under section 10(10AA) cannot be claimed by Mr. Ganesh in respect of leave encashment received by him while in service from his employer.