AMENDMENTS MADE BY FINANCE ACT, 2014- RELEVANT FOR MAY 2015/NOV 2015 EXAM

FEW AMENDMENTS RELATING TO CHARITABLE TRUSTS OR INSTITUTIONS

1. SECTION 11(6) & 11(7)-EFFECTIVE FROM A.Y.2015-16

Applicable to Charitable Trust/Institutions claiming exemption under section 11 to 13

PRACTICAL

During previous year, a public charitable trust registered under section 12AA of I.T. Act, for the concerned previous year, derived gross income of Rs. 26 lakhs, which consists of the following:

Sr. No.	Particulars	Amount (Rs.)
1.	Income from properties held under trust	9,00,000
2.	Voluntary contributions from public	7,00,000
3.	Corpus donations	4,00,000
4.	Dividend income from shares of Indian Companies	1,00,000
5.	LTCG on sale of shares (subject to security transaction tax)	3,00,000
6.	Income from agriculture operations	2,00,000

During the previous year, the trust had spent Rs. 11,60,000 towards charitable purposes. Further, Trust has purchased small office on 01-04-2014 for Rs. 5,00,000.*(Rate of depreciation is 10%).* Determine the taxable income of the trust.

Before, we go to the solution, let us comprehend amendment first.

There are two amendments affecting this practical.

1st Amendment :- Section 11(7)

Where a trust or an institution has been granted registration for purposes of availing of exemption under section 11, then such trust or institution cannot claim any exemption under any provision of section 10 except exemption relating to agricultural income and exemption under section 10(23C).

<u>That means,</u> as per this amendment, trust or institution registered under section 12AA can claim only following exemptions under section 10.

(i) *Section 10(1) : Exemption in relation to agricultural income*

(ii) *Section 10(23C): Exemption to certain national funds, educational institutions and hospitals.*

Therefore, reader shall strictly note that *trust or institution cannot straightaway exclude following incomes while computing total income* because such incomes are not covered by section 10(1) or 10(23C):-

Section 10(34)	:	Dividend Income
Section 10(38)	:	Long Term Capital Gain
Section 10(33)	:	Capital gain on transfer of unit of US 64
Section 10(34A)	:	Capital gain on Buy Back of unlisted shares
And many more …..	:	As covered by section 10 of the Income Tax Act, 1961

2nd Amendment :- Section 11(6)

Before, we digest this amendment, let's understand controversy first.
Controversial Issue:-Can the assessee, being a charitable institution, claim depreciation under section 32 in respect of an asset, where the cost of such asset has been treated as application of income for charitable purposes under section 11(1)(a)?

- **Answered in favour of Taxpayer**
  It was held by Bombay High Court that 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 past years.

- ***Answered against the taxpayer***
  It was held by Kerala High Court that once the expenditure on acquisition of assets has been treated as application of income for charitable purposes under section 11(1)(a), the full value of the asset stands written off and if depreciation is further allowed, the same will result in double deduction of capital expenditure leading to violation of provision of section 11(1) and therefore, the trust is not eligible to claim depreciation on such capital expenditure, in the current year or in any subsequent year. ***Lissie Medical Institutions v. CIT (2012) 348 ITR 344 (Ker.)***

Controversy set right by Finance Act, 2014
To set right above controversy, sub-section 6 has been inserted by section 11 as under:-

SECTION 11 (6) OF THE INCOME TAX ACT

"In this section where any income is required to be applied or accumulated or set apart for application, then, for such purposes the income shall be determined without any deduction or allowance by way of depreciation or otherwise in respect of any asset, acquisition of which has been claimed as an application of income under this section in the same or any other previous year."

That means, while determining total income of the trust, no depreciation shall be allowed in respect of an asset, cost of which has been claimed as an application of income, in the same or any other previous year.

SOLUTION

In this practical aspect, trust has purchased small office. Therefore, trust has two options:

Option 1: To claim investment in office as application of income and therefore, cannot claim depreciation in view of section 11(6) [amendment made by Finance Act, 2014]

Option 2: Not to claim investment in office as application of income and to avail depreciation in respect of such office.

Considering above two options, answer is as under**:**

Option 1

	Particulars	Amount (Rs.)
	Income from property held under trust	9,00,000
Add:	Voluntary Contribution received from public	7,00,000
Add:	Corpus Donations are not an income	Nil
Add:	Dividend income from shares (Exemption under section 10(34) not available in view of amendment discussed above)	1,00,000
Add:	LTCG on sale of shares (Exemption under section 10(38) not available in view of amendment discussed above)	3,00,000
Add:	Income from Agricultural Operations (Exemption under section 10(1) is available to trust)	Nil
		20,00,000
Less:	15% Set apart	(3,00,000)
Less:	Applied for the objects of Trust	(11,60,000)
Less:	Applied for purchase of Office	(5,00,000)
	Total Income	**40,000**

Option 2

	Particulars	Amount (Rs.)
	Income from property held under trust	9,00,000
Add:	Voluntary Contribution received from public	7,00,000
Add:	Corpus Donations are not an income	Nil
Add:	Dividend income from shares (Exemption under section 10(34) not available in view of amendment discussed above)	1,00,000
Add:	LTCG on sale of shares (Exemption under section 10(38) not available in view of amendment discussed above)	3,00,000

Add:	Income from Agricultural Operations (Exemption under section 10(1) is available to trust)	Nil
		20,00,000
Less:	Depreciation in respect of Office [10% of Rs.5,00,000]	(50,000)
	Balance	19,50,000
Less:	15% Set apart	(2,92,500)
Less:	Applied for the objects of Trust	(11,60,000)
	Total Income	**4,97,500**

SECTION 10(23C) -EFFECTIVE FROM A.Y.2015-16

2. Meaning of "Substantially financed by the Government" for the purpose of exemption under sub-clauses (iiiab) and (iiiac) of section 10(23C) and other two amendments related to section 10(23C)

PRACTICAL

Raksha Shakti University is claiming exemption under section 10(23C) (iiiab) since inception. During previous year 2014-15, its gross receipts is Rs.3.8 crore, break up of which is as under:-

Sr. No.	Particulars	Amount (Rs. In crores)
1.	Collection of Fees	2.00
2.	Government Grant	1.60
3.	Voluntary Contributions	0.20

In the course of assessment proceedings, Assessing Officer denies exemption under section 10(23C)(iiiab) on the ground that it is not a substantially financed university by the Government. Verify the correctness of stand taken by assessing officer.

Before, we go to the solution, let us comprehend amendment first.

The existing provisions of section 10(23C) (iiiab) and 10 (23C) (iiiac) provide exemption in respect of income of certain educational institutions, universities and hospitals which exist solely for educational purposes or solely for philanthropic purposes and not for purposes of profit and which are wholly or substantially financed by the Government.

The word "substantially financed by the Government" has not been defined in the Act. Moreover, judicial rulings do not give any concrete interpretation which can be adopted uniformly in different set of circumstances.

Therefore, section 10(23C) has been amended as under:-

“Any university or other educational institution, hospital or other institution shall be considered as being substantially financed by the Government for any previous year, if the Government grant to such university or other educational institution, hospital or other institution exceeds such percentage of the total receipts including any voluntary contributions, as may be prescribed, of such university or other educational institution, hospital or other institution, as the case may be, during the relevant previous year.”

In short, percentage of Government grant received during the previous year as to Total receipts (including voluntary contribution) has been taken as a base to decide whether entity is substantially financed by Government.

Further, Notification No. 79 dated 12th December, 2014 had prescribed **50%** for the purpose of section 10(23C) (iiiab) and 10 (23C) (iiiac).

SOLUTION

In case of Raksha Shakti University, for the previous year 2014-15, percentage of Government Grants as to **total receipts including voluntary contributions** comes to 42.10% [1.60 crore ÷ 3.80 crore] which is not exceeding 50%. Therefore, it is not a substantially financed university for the purpose of section 10(23C)(iiiab). Therefore, stand taken by assessing officer is correct.

Further, following two amendments are also made to section 10(23C) which are as under:-

1st Amendment

Further, law has been amended to provide that “other charitable trusts, universities, hospitals, charitable organization approved by specified authority for the purpose of section 10(23C)” can claim only following exemptions under section 10.

- **(i) Section 10(1) : Exemption in relation to agricultural income**
- **(ii) Section 10(23C): Exemption to certain national funds, educational institutions and hospitals.**

Note:-Above amendment is similar to section 11 (7)

2nd Amendment

Further, section 10(23C) has been amended to provide that while determining total income of various entities eligible to claim exemption under section 10(23C), no depreciation shall be allowed in respect of an asset, cost of which has been claimed as an application of income, in the same or any other previous year.

Note:-Above amendment is similar to section 11(6)

3.	**SECTION 12A -EFFECTIVE FROM 1ST OCTOBER, 2014**
	Benefit of section 11 and 12 shall be made available to trust or institution for the earlier yeas also even though registration has been obtained later

PRACTICAL 1

ABC Charitable trust was registered with Charity Commissioner on 10-12-08. But it failed to get registered with Commissioner of income tax under section 12AA of the Act. This trust had never filed income tax returns. For previous year 2013-14, it received notice under section 142(1) to file the return on or before 31-12-2014. Therefore, trust made an application to Commissioner of income tax for registration under section 12AA of the Act on 12.12.2014. Pending registration, trust filed the income tax return for the previous year 2013-14. The case of trust was selected for scrutiny. In mean time, it obtained registration from Commissioner on 15.01.2015.
Assessing officer would like to take following actions:-

(i) He wants to grant exemption under section 11 with effect from Previous year 2014-15 and onwards. Therefore, he denies benefit of exemption under section 11 for the previous year 2013-14.
(ii) He wants to give notice under section 148 for earlier six assessment years on the ground that trust had not been registered section 12AA and therefore, it is liable to tax for earlier six assessment years without taking exemption under section 11.

Is assessing officer justified in taking above actions?

PRACTICAL 2

Does your answer differ if trust had applied for registration in previous year 2009-10 but registration was refused by Commissioner of Income Tax?

Before, we go to the solution, let us comprehend the provisions of section 12A and 12AA in detail.

Conditions for claiming exemption under section 11 and Registration of Trust [Section 12A and 12AA]

- **Procedure**

  Every trust or institution shall submit an application for registration in the prescribed form [Form 10A] to the Commissioner of Income-tax.

  On receipt of the application, according to the provisions of Sec. 12AA which prescribe the procedure for registration, the Commissioner shall call for such documents or information as considered necessary in order to satisfy about the genuineness of activities of the trust or institution. Inquiries can also be made as deemed necessary.

  After being satisfied about the objects and the genuineness of activities an order shall be passed in writing, registering the trust or institution. If not so satisfied, an order shall be passed in writing, refusing to register. Copy of any such order shall be sent to the applicant. Before an order is passed refusing registration, reasonable opportunity of being heard should be given.

  The time limit for passing an order is six months from the end of the month in which the application is received.

- **Applicability of section 11 and 12**

  The trust is eligible for exemption u/s 11 and 12 from the financial year in which the application is made.

W.e.f. 1st October, 2014 following three proviso has been inserted under section 12A(2)

- **Circumstance when exemption would be granted for an earlier assessment year: (1st Proviso)**

  Provided *that where registration has been granted to the trust or institution under section 12AA, then, the provisions of sections 11 and 12 shall apply in respect of any income derived from property held under trust of any assessment year preceding the aforesaid assessment year, for which assessment proceedings are pending before the Assessing Officer as on the date of such registration and the objects and activities of such trust or institution remain the same for such preceding assessment year,*

  As per this proviso, once registration has been granted to trust or institution, it will get benefit of section 11 and 12 for earlier years also for which assessment proceedings are pending before the assessing officer on the date of such registration provided activities of such trust or institution remain the same for such earlier years.

- **Reassessment proceedings not to be initiated for earlier years due to reason of non-registration: (2nd Proviso)**

Provided further *that no action under section 147 shall be taken by the Assessing Officer in case of such trust or institution for any assessment year preceding the aforesaid assessment year only for non-registration of such trust or institution for the said assessment year.*

As per this proviso, once registration has been granted to trust or institution, no action under section 147 shall be taken by the assessing officer for earlier assessment years only for want of registration.

- **Non-availability of above benefits to a trust or institution in certain cases: (3rd Proviso)**

Provided also *that provisions contained in the first and second proviso shall not apply in case of any trust or institution which was refused registration or the registration granted to it was cancelled at any time under section 12AA.*

The benefit of earlier two proviso are not available if trust or institution was refused registration in past or registration granted to them was cancelled in past.

SOLUTION 1

(i) As per provisions of the Income Tax Act, the trust is eligible for exemption u/s 11 and 12 from the financial year in which the application is made. Therefore, trust can claim exemption under section 11 from previous year 2014-15 and onwards because it made an application on 12-12-2014.

But in view of first proviso inserted to section 12A(2), the benefit of sections 11 and 12 shall also be available for preceding previous years, provided the objects and activities of the trust remain the same for such preceding years.

Considering this amendment, the assessing officer is not justified in refusing exemption for the previous year 2013-14.

(ii) Primarily assessing officer is empowered to issue notice under section 148 if he has reason to believe that income has escaped assessment.

But in view of second proviso to section 12A(2), *no action under section 147 shall be taken by the Assessing Officer in case of such trust or institution for any assessment year only for non-registration of such trust or institution for the said assessment year.*

Considering this, Assessing officer is not justified in initiating action under section 147 by issuing notice under section 148.

SOLUTION 2

Considering third proviso to section 12A(2), benefit of first proviso (exemption under section 11 is available for earlier years) and benefit of second proviso (the assessing officer will not re-open cases of earlier years under section 147) is available only when trust or institution had not been refused registration in past or its registration had not been cancelled in past.

But in the given case, trust was refused registration in previous year 2009-10, therefore, considering the effect of third proviso, assessing officer is correct in taking both the actions.

SECTION12AA-EFFECTIVE FROM 1ST OCTOBER 2014

4. Power of Principal Commissioner/Commissioner to cancel registration of trust or institution expanded

PRACTICAL

Ram-Lakhan Charitable trust is a registered trust under Income Tax Act. During the course of assessment proceedings for the assessment year 2013-14, the assessing officer found that activities of trust are genuine and not in contravention of the objects of trust but made following observations:

(i) Remuneration paid to trustees is more than what shall be reasonably paid for such services.
(ii) Property of the trust was made available to trustee without charging rent.

As a result, the assessing officer had given show cause notice that why exemption of trust shall not be withdrawn applying section 13(1)(c) and why trust shall not be taxed at maximum marginal rate? Trustees of the trust failed to give explanation and therefore, assessing officer forfeited exemption of trust while passing order under section 143(3).

Based on the above assessment order, Commissioner issued notice to Ram Lakhan Charitable trust that why registration of trust shall not cancelled?

The contention of trustees was that the activities carried out by the trust are genuine and same fact has also been noted by the assessing officer while passing order under section 143(3), therefore in view of provisions of section 12AA(3), Commissioner is not justified in cancelling registration of trust.

Examine the validity of stand taken by trustees.

Before, we go to the solution, let us comprehend the provisions of section 12AA in detail.

- **Cancellation of registration - Sec. 12AA (3)**
  Where a Trust or an Institution has been granted registration and subsequently the Commissioner is satisfied that the activities of such trust or Institution are not genuine or in contravention of the objects, then the Commissioner has the power to pass an order in writing canceling the registration after giving a reasonable opportunity of being heard.

- **Cancellation of registration – Section 12AA (4) (Inserted by FA 2014 w.e.f. 1st October, 2014)**

Without prejudice to the provisions of sub-section (3),

where

a trust or an institution has been granted registration under section 12AA/ 12A

and

subsequently it is noticed that the activities of the trust or the institution are being carried out in a manner

that

the provisions of sections 11 and 12 do not apply due to operation of sub-section (1) of section 13,

then,

the Principal Commissioner or the Commissioner may by an order in writing cancel the registration of such trust or institution:

Provided *that the registration shall not be cancelled under this sub-section, if the trust or institution proves that there was a reasonable cause for the activities to be carried out in the said manner.*

SOLUTION

On reading section 12AA(3), Commissioner has power to cancel registration only if activities of trust are not genuine or in contravention of the objects but with effect from 1st October, 2014, Commissioner is empowered to cancel registration of trust under section 12AA(4) if activities of trust are carried out in a manner that exemption under section 11 is not available in view of section 13(1) of the Act.

In the present case, assessing officer forfeited exemption under section 11 applying section 13(1)(c) because remuneration paid to trustees was unreasonable and property of trust is made available without charging adequate rent. And therefore, considering the provisions of section 12AA(4), Commissioner is justified in cancelling registration of trust.

Hence, the contention raised by trustees does not find legal support but trustees, alternatively, may plea to CIT that there was a reasonable cause for paying higher remuneration or making property available without charging rent.

	SECTION 115BBC-EFFECTIVE FROM A.Y. 2015-16
5.	**Taxability of anonymous donations exempt from applicability of maximum marginal rate of tax**

PRACTICAL

A trust, established wholly for charitable purpose, received voluntary contributions of Rs.100 lakh during the previous year, out of which Rs.40 lakh were anonymous donations. It applied Rs.48 lakh for the purposes of the trust during the year. Compute the tax payable by trust

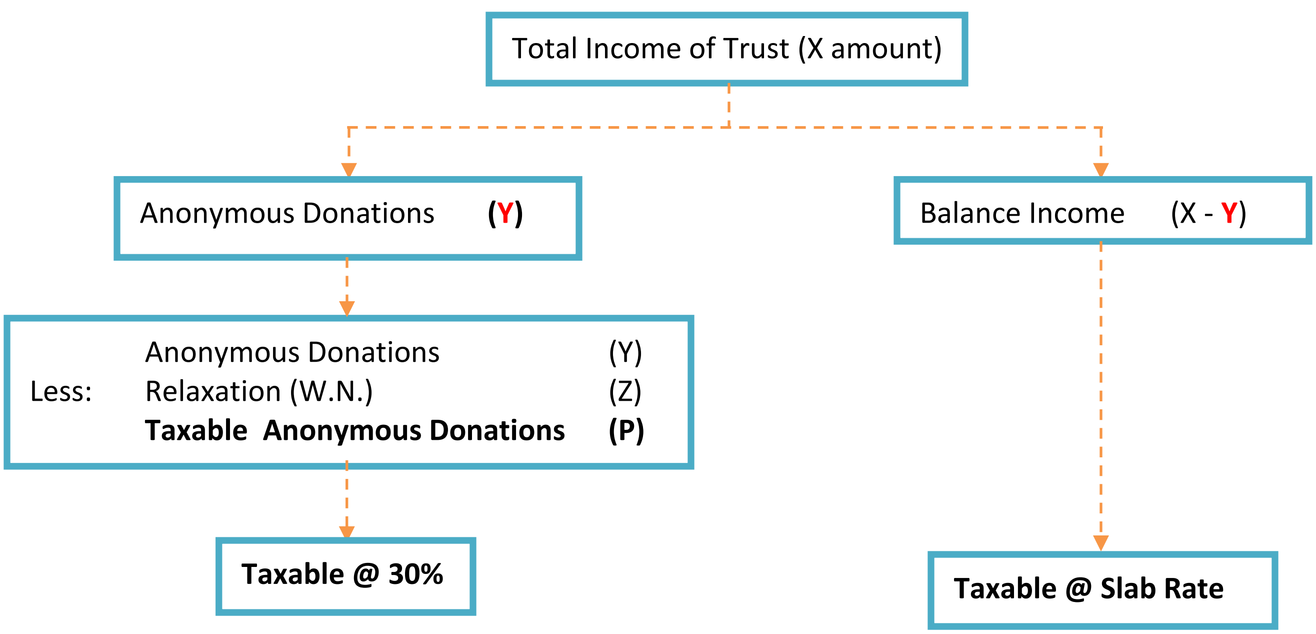
(i) Before amendment (For the A.Y. 2014-15)
(ii) After amendment (For the A.Y. 2015-16)

Before, we go to the solution, let us comprehend the provisions of section 115BBC in a chart form.

Taxability of anonymous donations exempt from applicability of maximum marginal rate of tax

<u>Before amendment:-</u>

Provisions of Section 115BBC before amendment (Applicable upto A.Y. 2014-15)



Working Note:

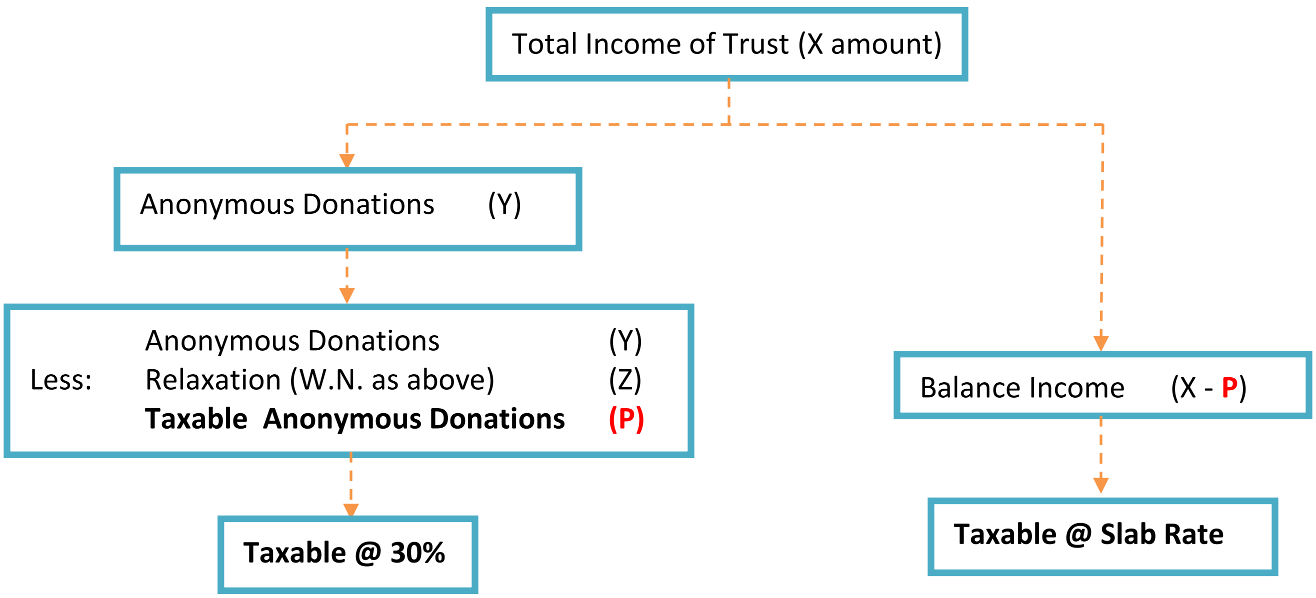
Relaxation given under section 115BBC shall be higher of the followings

(a) 5% of TOTAL DONATIONS

(b) Rs. 1,00,000

<u>After amendment:-</u>

Provisions of Section 115BBC after amendment (Applicable from A.Y. 2015-16)



SOLUTION

Computation of total income of trust

	Particulars	Amount Rs.
	Voluntary contributions (excluding anonyms donations)	60,00,000
Less:	15% set apart for future	(9,00,000)
	Balance	51,00,000
Less:	Applied for the object of the trust	48,00,000
	Balance	3,00,000
Add:	Anonyms donation	40,00,000
	Total Income of the trust	**43,00,000**

Tax calculation for the A.Y. 2014-15

Total Income of Trust (43Lakhs)

Anonymous Donations **(40 Lakhs)**

Balance Income (43Lakhs – **40 Lakhs**)
3 Lakhs

	Anonymous Donations	40 Lakhs
Less:	Relaxation (W.N.)	5 Lakhs
	Taxable Anonymous Donations	**35 Lakhs**

Taxable @ 30%

Taxable @ Slab Rate

Tax =10,50,000

Tax = Rs.5,000

Tax Liability

	Tax	10,55,000
Add:	Education Cess (3%)	31,500
	Tax Liability	**10,81,500**

Working Note:

Relaxation given under section 115BBC shall be higher of the followings

(a) 5% of TOTAL DONATIONS
5% of 100 Lakhs
Rs. 5,00,000

(b) Rs. 1,00,000

Tax calculation for the A.Y. 2015-16

Total Income of Trust (43 Lakhs)

Anonymous Donations **(40 Lakhs)**

	Anonymous Donations	40 Lakhs
Less:	Relaxation (W.N. as above)	5 Lakhs
	Taxable Anonymous Donations	**35 Lakhs**

Balance Income (43 Lakhs – **35 Lakhs**)
8 Lakhs

Taxable @ 30%

Tax =10,50,000

Taxable @ Slab Rate

Tax = Rs.85,000

Tax Liability

	Tax	11,35,000
Add:	Education Cess (3%)	34,050
	Tax Liability	**11,69,050**

Few more files on amendments made by Finance Act 2014 will be made available soon on CA CLUB website.