



**PROPOSALS UNDER THE FINANCE BILL 2023 AND IMPACT OF  
THE RECENT SUPREME COURT DECISIONS IN RELATION TO  
CHARITABLE TRUSTS**

## 1. Time limit of 5 years for refurbishing of corpus

The Finance Act 2021 had amended Section 10(23C) and Section 11 of Income Tax Act, 1961 ('the Act'), to prevent claiming application of corpus as application of income by charitable institution. Accordingly, charitable trusts were not allowed to treat application of corpus as application of income unless the corpus is refilled or reinstated by the charitable institution. Similarly, vide the said amendment, charitable institutions were also prevented from claiming application of borrowed money/ loan as application of income, unless there is repayment of such borrowed money/ loan by the charitable institution, in which case it would be considered as application of income.

The Finance Bill 2023 further imposes a cap of **5 years** for refurbishing of corpus and repayment of loan. Thus, in order to claim the repayment of loan as application of income, the loan would have to be repaid within a period of five years. This was done to curb the availability of indefinite period for the investment or depositing of funds back to corpus or repayment of loan that would make the implementation of provisions difficult, the cap of 5 years has been proposed.

The amendment will take effect from **1 April 2023** and will apply to **assessment year ('AY') 2023-24**.

## 2. Donation to other trusts

Charitable trusts or institutions are required to apply 85% of their income for the charitable or religious purposes for which it was set up and thus, accumulating only a maximum of 15% of income received.

The scope of 85% applicability encompassed one trust giving donation to another trust which was aligned with its objectives. However, this led to the creation of a chain of trusts making donations to one another, accumulating 15% at each stage, and the effective application towards the religious or charitable purpose getting reduced significantly.

*For example, Trust A may donate 85% of its income to Trust B, which aligned with its objectives. Trust B may retain 15% percent of such 85% donation received from Trust A and donate the remaining to Trust C. Thus, at each stage 15% gets retained thereby reducing the amount available for actual application to the religious or charitable cause.*

In order to curb such instances, the Finance Bill 2023 proposes to restrict the amount of donation one trust makes to another trust to 85% of the eligible donations. Thus, only 85% of the eligible donations made by a trust or an institution to another trust or institution shall be treated as application of income only to the extent of 85% of such donation.

The proposed provisions are unclear on whether the limit of 85% is applicable item-wise on each donation made to another charitable trust or on the aggregate donations made to other charitable trust. For now, given the intent behind the proposal stated in the memorandum to Finance Bill 2023, it may be safer to interpret that the limitation of 85% is applicable item-wise on each donation made to another charitable trust.

Accordingly, the Finance Bill 2023 proposes relevant amendments which will take effect from **1 April 2024** and shall be applicable from **AY 2024-25**.

## 3. Meaning of "specified violation" under Section 12AB and Section 10(23C).

Taxation & Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 ('TOL Act') had substantially amended the provisions for application and registration of trusts. As per the amended provisions, the new trusts are required to apply for provisional registration/ approval which is valid for 3 years or till six months from commencement of activities, whichever is earlier. The trusts already registered were required to furnish an application under Form 10A for re-registration/ approval on the e-filing portal, wherein the provisional approval/ registration or approval/ registration is granted in an automated manner without verification.



The said approval/ registration and the provisional approval/ registration can be cancelled by the specified authorities for certain specified violations.

In furtherance of the same, the Finance Bill 2023 proposes to expand the scope of specified violations under Section 10(23C) as well as Section 12AB of the Act **to include the case where the application furnished on the e-portal is incomplete or the information contained false or incorrect information.**

This has been done with the intent to curb instances where the form is furnished by the trusts for provisional registration or re-registrations, which get automated approval on the e-portal.

The amendment to Section 10(23C) and Section 12AB of the Act will take effect from **1 April 2023**.

#### 4. Levy of exit tax on non-filing of application

Exit tax is levied under Chapter XIII - EB of the Act (Sections 115TD, 115TE and 115TF) when the organisation is converted into a non-charitable organisation or gets merged with a non-charitable organisation or is a charitable organisation with dissimilar objects or does not transfer the assets to another charitable organisation. The exit tax liability is provided under Section 115TD(5) of the Act, which states as under:

*' The principal officer or the trustee of the trust or the institution, as the case may be, and the trust or the institution shall also be liable to pay the tax on accreted income to the credit of the Central Government..'*

Further, the amendments brought in by TOL Act are as follows:

- All the existing trusts are required to apply for re-registration/ approval by the due date;
- New trusts and institutions are required to apply for provisional registration/ approval at least one month prior to the commencement of the previous year

In case a charitable trust or institution deems certain income to be applied, such trust or

relevant to the AY from which the said registration/approval is sought. Such provisional registration/approval shall be valid for a period of 3 years.

- Provisionally registered/approved trusts and institutions again need to apply for regular registration/approval at least six months prior to expiry of the period of the provisional registration/approval or within six months of the commencement of activities, whichever is earlier.
- The trusts and institutions are required to apply at least six months prior to the expiry of re-registration/approval.

The Finance Bill 2023 proposes that provisions of Chapter XIII - EB shall be applicable on trusts or institutions failing to make an application for registration/ approval, provisional registration/ approval or re-registration/ approval, as the case maybe, as mentioned above. Accordingly, exit tax shall be levied on such trusts or institutions. The date of conversion of the trust or institution shall be considered to be the last date for making an application for registration. In this respect, the liability of the principal officer or trustee shall continue as already provided under Section 115TD(5) of Act and no changes in relation to liability of such principal officer or trustees with respect to exit tax have been proposed in this Finance Bill 2023.

The proposed amendment will take effect from **1 April 2023** and will apply to **AY 2023-24** and subsequent AYs.

#### 5. Alignment of time limit for furnishing of Form 10A and Form 9A

Charitable trusts and institutions registered under Section 10(23C) as well Section 12AB of the Act are required to get their accounts audited as per the relevant provisions.

Further, where a charitable trust or institution accumulates or sets apart its income, such trust or institution is required to furnish a statement in prescribed Form 10 on or before the due date specified for furnishing return of income under Section 139(1) of the Act.

institution are required to furnish a statement in prescribed Form 9A, also to be filed at



the same time as income tax return under Section 139(1) of the Act.

The Finance Bill 2023 proposes to change the said due date for filing Form 10 or Form 9A to at least **two months prior to the date due date of filing income-tax return** under Section 139(1) of the Act. This is done so as to align the dates of filing Form 10 and Form 9A with the due date of filing the audit report, which is one month before the due date of filing the income-tax return under Section 139(1), considering auditors are required to report details of Form 10 and 9A in the audit report also.

The amendment in the due date shall take effect from **1 April 2023** and will accordingly apply for **AY 2023-24**.

#### 6. Denial of exemption where return of income is not furnished within time.

The Finance Act 2022 had inserted sub-section 8A to Section 139 of the Act, wherein it had provided an option to the taxpayers to furnish updated return of income up to 2 years from the end of the AY i.e. revised return.

However, the Finance Bill 2023 further clarifies that that the exemption under Section 10(23C), Section 11 and Section 12 of the Act shall be available only if the return of income is filed within the timelines prescribed under Section 139(1) i.e. time limit for filing income-tax return or 139(4) i.e. time limit for filing belated return. In case of revision of return under sub-section (8A) of Section 139, the exemption shall not be available.

The amendment will take effect from **1 April 2023** and apply in relation to **AY 2023-24**.

#### 7. Amending timelines for applying for provisional and final registrations

As stated above, the new trusts and institutions are required to apply for provisional registration/ approval at least one

month prior to the commencement of the previous year relevant to the AY from which the said registration/approval is sought. Further, provisionally registered/approved trusts and institutions again need to apply for regular registration/approval at least six months prior to expiry of the period of the provisional registration/approval or within six months of the commencement of activities, whichever is earlier.

However, this would lead to a situation where trusts or institutions formed or incorporated in one financial year would not be able to get exemption in that year in which they are formed or incorporated, if they had not applied for the same one month before the financial year in which exemption was being sought. Further, trusts or institutions whose activities had already commenced, are required to apply for two registrations (provisional and regular) simultaneously.

In order to address this difficulty, the Finance Bill 2023 proposes that the trusts or institutions which are applying for registration prior to commencement of activities may apply for provisional registration only before commencement of activities. Further, the trusts or institutions which have already commenced their activities shall make an application for regular registration directly, as against provisional registration.

The applications filed shall be examined by the Principal Commissioner or Commissioner as per the prescribed procedure and where the Principal Commissioner or Commissioner is satisfied about the objects and genuineness of the activities and compliance, registration or approval shall be granted for 5 years. The Principal Commissioner or Commissioner shall pass an order granting or rejecting such application within 6 months calculated from the end of the month in which the application was received.

The amendments shall take effect from **1 October 2023**.



Summary of latest Supreme Court ("SC") decisions in relation to charitable trusts

Trusts/institutions registered under section 10(23C) of the Act <sup>1</sup>	Trusts registered under section 12AB of the Act (having specific charitable objects/ <i>per se</i> category)	Trusts registered under section 12AB of the Act having main object of advancement of general public utility
<p>Trusts covered under clauses<sup>2</sup> -</p> <p><b>(iiiad)/(vi)</b> - university or other educational institution existing <b>solely for educational purposes</b></p> <p><b>(iiiiae)/(via)</b> - any hospital or other institutions<sup>3</sup> existing <b>solely for philanthropic purposes</b></p>	<p>All Charitable institutions (trust/society/section 8 company) having the following charitable purpose<sup>4</sup> and carrying out the following -</p> <ul style="list-style-type: none"> <li>• relief of the poor,</li> <li>• education,</li> <li>• yoga,</li> <li>• medical relief,</li> <li>• preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest</li> </ul>	<p>All charitable institutions having the object of <b>advancement of any other object of general public utility ("GPU entities")</b> and carrying out the object.</p>
<p><b><u>Meaning of 'education'</u></b></p> <p>The Hon'ble SC in <b>New Noble Educational Society -vs.- CCIT</b> (Civil Appeal No. 3795 of 2014 dated 19 October 2022) after considering its own decision<sup>5</sup> held that for the purposes of definition of "charitable purpose" under section 2(15) of the Act, <b>'education' means</b></p>	<p>The meaning of the term 'education' as per the SC decision in <b>New Noble Educational Society (supra)</b> shall also be applicable to trusts registered under section 12AB of the Act having <i>per se</i> objects, being education.</p>	<p>The SC in <b>ACIT -vs.- Ahmedabad Urban Development Authority</b> (Civil Appeal No. 21762 of 2017 dated 19 October 2022) has held that the proviso<sup>6</sup> to section 2(15) of the Act and the restrictive condition of eschewing activities of profit does not apply to</p>

<sup>1</sup> Act means the Income Tax Act, 1961

<sup>2</sup> This note does not cover institutions substantially financed by the Government (clauses (iiiab) and (iiiac)) and institutions having other charitable purposes (clause (iv)) or religious purposes (clause (v)) under section 10(23C) of the Act

<sup>3</sup> "for the reception and treatment of persons suffering from illness or mental defectiveness or for the reception and treatment of persons during convalescence or of persons requiring medical attention or rehabilitation"

<sup>4</sup> "Charitable purpose" is defined under section 2(15) of the Act

<sup>5</sup> Loka Shikshana Trust v. Commissioner of Income Tax, (1976) 1 SCC 254.

<sup>6</sup> "Provided that the advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income from such activity, unless—

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

(ii) the aggregate receipts from such activity or activities during the previous year, do not exceed twenty per cent of the total receipts, of the trust or institution undertaking such activity or activities, of that previous year;"



Trusts/institutions registered under section 10(23C) of the Act <sup>1</sup>	Trusts registered under section 12AB of the Act (having specific charitable objects/ <i>per se</i> category)	Trusts registered under section 12AB of the Act having main object of advancement of general public utility
<u>imparting formal scholastic learning.</u>		<i>per se</i> categories.
<p><b><u>Meaning of 'solely'</u></b></p> <p>The SC while dealing with the word 'solely' in section 10(23C) of the Act has held that the word 'solely' means <b><u>'only' or 'exclusively' and hence 'solely' is not same as 'predominant/mainly'</u></b>.</p> <p>The interpretation of seventh proviso to section 10(23C)(vi) of the Act is that the charitable institution must <i>solely</i> exist for the educational object and not for profit. Hence, a trust or educational institution, which seeks approval or exemption, <b><u>should solely be concerned with education, or education related activities. If, incidentally, while carrying on those objectives, the trust earns profits, it has to maintain separate books of account.</u></b></p>	<p>The term 'solely' is not used in section 2(15) of the Act and hence the same is not applicable to the entities registered under section 12AB of the Act.</p> <p>However, the SC in <b><i>Ahmedabad Urban Development Authority (supra)</i></b> has defined '<b>charitable purpose</b>' and charity as providing goods or services -</p> <ul style="list-style-type: none"> <li>• at no consideration or</li> <li>• at cost or</li> <li>• at nominal consideration</li> </ul> <p>Hence, the <i>per se</i> categories entities cannot charge substantial amounts - over and above the cost it incurs for doing the same work. If the services are provided far above the cost-plus nominal mark-up, then such activities are in the nature of trade, commerce or business. It is be noted that the decision of the SC in <b><i>Queen's Education</i></b> has allowed the <i>per se</i> charity institutions to earn profit upto 15% for carrying out its main objects.</p> <p>However, any other activities other than the main object, the said activities shall have to qualify the following -</p> <ul style="list-style-type: none"> <li>• It should be incidental to the attainment of the main object, i.e., the same should be conducted actually in the course of attainment of main object and</li> <li>• Should not record substantial</li> </ul>	<p>For GPU entities, activity in the nature of trade, business or commerce is not permissible anymore. However, if the same is for actual carrying on of advancement of GPU objects and not exceeding 20% of the total receipts, then exemption can be claimed. However, the condition of maintaining separate books of accounts is applicable.</p>



Trusts/institutions registered under section 10(23C) of the Act <sup>1</sup>	Trusts registered under section 12AB of the Act (having specific charitable objects/per se category)	Trusts registered under section 12AB of the Act having main object of advancement of general public utility
	<p>profits (subject to <b>Queen's Education</b>).</p> <p>The terms 'business' or 'in the nature of business' have been interpreted by the SC as under after referring to the decision of <b>Director of Civil Supplies</b><sup>7</sup> -</p> <p><i>"To regard an activity as business, there must be a course of dealings, either actually continued or contemplated to be continued with a profit- motive; there must be some real and systematic or organised course of activity or conduct with a set purpose of making profit. To infer from a course of transactions that it is intended thereby to carry on business ordinarily there must exist the characteristics of volume, frequency, continuity and system indicating an intention to continue the activity of carrying on the transactions for a profit. But no single test or group of tests is decisive of the intention to carry on the business. "</i></p> <p>It is however to be noted that if the activity is only recovering the cost and has marginal mark-up, then it is not in the nature of business at all.</p>	

**Powers of Prescribed Authority while granting approval for registration under section 10(23C)**

The SC has held that the *Prescribed Authority* (the Commissioner or any other prescribed authority) has the discretion to look into the past history of accounts, and to find out

whether the applicant is engaged in fact solely in education.

Further, the *Prescribed Authority*, while considering the application for approval and further material called for should confine the inquiry ordinarily to the nature of the income earned and whether it is for education or education related objects of the charitable institutions.

<sup>7</sup> *Director of Civil Supplies v. Member Board of Revenue 1967 (3) SCR 778*

### Applicability of Other Laws

The SC has made it clear that charitable institutions and societies which may be regulated by other state laws, must comply with them just as in the case of laws regulating education (at all levels). Such compliance is also a relevant consideration for the Prescribed Authority in deciding applications for approval under section 10(23C).

### What is 'incidental' business activity in relation to education?

The SC has held that imparting education through schools, colleges and other such institutions would be *per se* charity. Apart from that there could be **activities incidental to providing education**, for example -

- textbooks,
- providing bus facilities to transport children,
- providing summer camps for pupils' special educational courses, such as relating to computers etc., which may benefit its pupils in their pursuit of learning.

It has been held that if charitable institutions provide their premises or infrastructure to other entities, trusts, societies, etc for the purposes of conducting workshops, seminars, or even educational courses and outsiders are permitted to enrol in such seminars, workshops, courses, etc. then the income derived from such activity cannot be characterised as part of education or 'incidental' to the imparting of education.

### Difference between business held under trust and business carried on by a trust

The SC has clarified the difference between section 11(4) and section 11(4A) of the Act. It has held that Section 11(4) applies to cases where the business undertaking itself is the property held by the trust. Thus, where the property held in trust, or where property settled by the donor or trust creator in the

favour of the trustees itself is a business undertaking, then the income from such undertaking is covered by section 11(4) of the Act. Whereas section 11(4A) states that when a trust carries on a business, unless the business is incidental to the attainments of the objects of the trust, it would be disentitled to an exemption under section 11(1). It imposes a further condition that separate books of accounts need to be maintained in such cases.

It is pertinent to note that the Income Tax Authorities have sought clarification regarding the decision of the SC in Ahmedabad Urban Development Authority (Supra) whether the said decision will enable the Income Tax Department to redo the assessments in accordance with the said decision for the past and examine the eligibility on a yearly basis for the future. **The SC has clarified vide order dated 3 November 2022<sup>8</sup> that the said decision shall apply for the assessment years in question, which were before the SC and were decided (wherever the appeals are decided against the Revenue) are to be treated as final. However, for future assessment years, which have not been decided by the SC, the concerned authorities shall apply the law laid down by the SC, having regard to the facts of each such assessment year.**

- Asim Choudhury (Partner), Kinjal Buaria (Senior Associate) and Akshara Shukla (Senior Associate)

<sup>8</sup> ACIT(Exemptions) -vs.- Ahmedabad Urban Development Authority (MA No. 1849 of 2022/Civil Appeal No. 21762 of 2017 dated 3 November 2022)

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