Standards & Norms

Resource support on NGO Governance, Accounting and Regulations

• Legal Series Vol. X • Issue 6 • September 2018

For private circulation only

SUPREME COURT RULING ON TREATMENT OF INTEREST ON CORPUS FUND



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A joint initiative of fmsf VANI

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OVERVIEW

1.1.1 Corpus donation received by any charitable or religious organisation should not be treated as a part of income.

1.1.2 Even in the case of organisations not registered under section 12AA, corpus donation received should not be treated as a part of income, in the light of the available judicial precedence.

1.1.3 In a recent case, the Supreme Court of India has decided that interest earned on corpus fund should not be treated as a part of income of the organisation.

1.1.4 It is advised that organisations should carefully draft the agreements and MoUs pertaining to corpus donation and restricted/project grant. For greater clarity a clause should be inserted allowing the interest earned on the corpus donation or restricted/project grant to be added back to such corpus fund or restricted/project fund.

TAXABILITY OF CORPUS DONATION IF A TRUST IS NOT REGISTERED UNDER SECTION 12AA

1.2.1 The corpus donation is normally treated as income and covered under the definition of '*income*' within the meaning of Section 2(24)(iia) of the Income Tax Act, 1961. In other words, it is treated as income and specifically exempted for organisations registered under se`ction 12AA of the Income Tax Act, 1961. It may be noted that section 12AA is the section under which the certificate of tax exemptions is granted to NGOs or Trusts.

1.2.2 Normally, it is believed that corpus donation will become taxable if an organization loses 12AA registration. However there is preponderance of judicial precedence to suggest that corpus donation cannot be taxed even if the organization does not

have 12AA registration.

LANDMARK RULING BY SUPREME COURT ON INTEREST EARNED ON CORPUS FUND

1.3.1 The corpus donations received are not included in the income of the organisation, however the interest earned on corpus fund, hitherto, was treated as a part of the income of the organisation. In other words all interest earned on corpus fund & restricted grant are included in the income of the organisation and are subject to 85% utilisation as required under the Income Tax Act 1961. However, the Supreme Court of India, recently, has given a landmark ruling with regard to the interest income on corpus donation.

1.3.2 In the case *Commissioner of Income-Tax. (Exemption), Kochi vs. Mata Amrithanandamayi Math Amritapuri* [2018] 94 taxmann.com 82 (SC) the Supreme Court of India held that where assessee received corpus donation on which it earned interest, in view of specific direction of donors that said interest would also form part of corpus, assessee's claim for exemption under section 11 in respect of interest so earned was to be allowed.

IMPORTANT CASES REGARDING NON TAXABILITY OF CORPUS DONATION

1.4.1 In the case of Income Tax Appellate Tribunal "D" Bench, Mumbai *Chandraprabhu Jain vs. Assistant Commissioner of Income Tax* I.T.A. No. 230/Mum/2016, order dated 12 -08-2016 reaffirmed that corpus donations cannot be taxed even if the Trust is not registered under section 12AA.

1.4.2 Similar view was taken by ITAT, Agra in the case of ***ITO v. Gaudiya Granth Anuved Trust*** reported in (2014) 48 taxmann.com 348(Agra-Trib) whereby Tribunal took a view that corpus donations cannot be taxed even if the Trust is not registered under section 12AA for the following reasons :

1. The religious endowments are not invalid on the ground that neither the temple

nor the image had been consecrated at the time of creating the endowments.

2. The assessees have to be assessed in the status of "individual" since they are artificial juridical entities and

3. The voluntary contributions received by the assessee towards the corpus cannot be brought to tax.'

1.4.3 In the case *Chandraprabhu Jain vs. Assistant Commissioner of Income Tax (supra)* it was submitted that by virtue of provisions of Section 11(1)(d) and Section 12(1) of the Act, donations received towards corpus of the trust/various funds shall not be deemed to be income derived from property held under trust wholly for charitable or religious purposes. It was submitted that receipt cannot be taxed as income unless it is an income within meaning of Section 2(24)(iia) of the Act read with Section 12 of the Act. Section 12 of the Act makes it clear that contributions made with a specific directions that they shall form part of the corpus of the trust or institution shall not be considered as income of the trust. The assessee also submitted that being AOP, by virtue of provisions of Section 56(2)(vii) of the Act, such receipts are not taxable in the hands of the assesse as income from other sources. It was also submitted that the AO also erred in taxing the assessee's income at maximum marginal rate in the status of AOP. It was submitted that no part of the income of the assesse is liable to be charged at maximum marginal rates since no part of the income of the assessee enures or is used or applied directly or indirectly for the benefit of specified category of persons referred to in Section 13(3) of the Act, that no part of the trust funds are invested in contravention of the investment pattern prescribed u/s 13(5) of the Act, the assessee trust is not engaged in the any business and the objects of trust is not to earn profit and to share among the members . The assessee relied upon the following case laws:-

1. *Peetadhipathi Trust, Mysore v. Department of Income Tax*, Bangalore ITAT ITA No. 1382 & 1535/Bang/2010.

2. *Sree Ramkrishna Samity v. DCIT* Cir. 2, Siligiri, ITA No. 1680 to 1685/2012 dated 9-10-2015.

3. *Gaudiya Granth Anuved Trust v. Department of Income Tax*, ITA No. 386/Agra/ 2012.

4. *Shri Shankar Bhagwan Estate v. Income Tax Officer* (Calcutta), [1997] 061 ITD 0196(Cal).

5. *Society for the promotion of Education, Adventure,Sports and Conservation of Environment v. CIT* (2008) 171 Taxmann 113(All.)

6. *Rev. Father Trust Oscar Colaso Memorial Medical Association v. CIT* (2009) 31 SOT 1(Mum.)

7. *R. B. Shreeram Religious & Charitable Trust v. CIT* (1988) 172 ITR 373(Bom)

THE LEGISLATIVE INTENT OF TREATING CORPUS DONATION AS INCOME

1.5.1 With regard to the interpretation that donations falls under the definition of income u/s 2(24)(iia) of the Act, it is worthwhile to state that income definition is an inclusive definition. An inclusive definition extends the specific meaning given in the stated items by the general meaning as commonly understood by the said expression which is defined in a statute. The word income as is commonly understood does not include any donation specifically meant for specific purposes or with specific direction. Further section 2(24) had undergone amendment by way of insertion of clause (iia) by Finance Act, 1972 with effect from 1.4.1973. In this connection, it will be relevant to get into the Memorandum explaining the provisions in Finance Act 1972 reported in 83 ITR (St.) 173, wherein Paragraphs 24 and 25 clearly define the scope of the amendment wherein in paragraph 25(i) , the concluding sentence is as under:-

> ***"contributions received with a specific direction that they will form part of the corpus of the trust or distribution will, however, not be regarded as income."***

Thus the relevant clause defining income in section 2(24)(iia) as introduced with effect from 1.4.1973 was clearly not intended to cover contributions / donations received with a specific direction that they will form part of the corpus of the trust for utilization in acquisition / construction of a capital asset. Thus what is not income as per the

definition of the word income in the Act cannot be brought to tax under any other provision of the Act. The text of section 2(24) of Income Tax Act, 1961 is provided in ***Annexure 1***.

1.5.2 The ITAT, Chennai in *Indian Society of Anaesthesiologists v. ITO* in decision reported in (2014) 47 taxmann.com 183(Chennai-Trib.) held that specific funds created for fulfilling specific objectives for which these separate funds are constituted remain as capital funds as the funds can be used for fulfilling specific objectives for which these funds are constituted and hence to be treated as corpus funds and to be excluded from computation of Income.

1.5.3 The ITAT, Bangalore in *ITO v. Vokkaligara Sngha* in a decision reported in (2015) 44CCH 0509(Bang. Trib.) whereby the Tribunal held that voluntary contributions received for a specific purpose cannot be regarded as income u/s 2(24)(iia) of the Act since they were capital receipts being corpus fund and tied up grants for specific purposes. In our considered view, keeping in mind our detailed discussions above & the case laws cited before us, these corpus donations of Rs.4,55,446/- received by the assessee trust cannot be brought to tax despite the fact that the assessee-trust was not registered u/s 12A/12AA of the Act.

1.5.4 In the case *ACIT vs. Nagarjuna Education Society*, [2011] 12 taxmann.com 375 (Visakhapatnam)/[2011] 46 SOT 501 (Visakhapatnam) the following was held by the tribunal:

(*a*) Direction that donation should form part of corpus should come from the donor and not the discretion of others.

(*b*) It does not depend on the sweet will of the donee/institution or other agencies.

(*c*) A.O. cannot change character from corpus to voluntary.

In the case *Dharma Pratishthanam* 11 ITD 40 (Delhi) it was held that "*There is no obligation to retain corpus forever and may be used for objects of the trust.*"

The hon'ble Income-tax Appellate Tribunal, Kolkata in the case of *Shri Shankar Bhagwan Estate v. ITO* [1997] 61 ITD 196 (Cal) in which, the taxability of corpus donation has been examined in the light of section 12 read section 2(24)(iia) of the Income-tax Act and in this decision, it has been held as under :

'So far as section 2(24)(iia) is concerned, this section has to be read in the context of the introduction of the present section 12 it is significant that section

2(24)(iia) was inserted with effect from April 1, 1973 simultaneously with the present section 12, both of which were introduced from the said date by the Finance Act, 1972. Section 12 makes it clear by the words appearing in parenthesis that contributions made with a specific direction that they shall form part of the corpus of the trust or institution shall not be considered as income of the trust. The Board's Circular No. 108 dated March 20, 1973 is extracted at page 1277 of Volume I of Sampath Iyengar's Law of Income-tax, 9th edn. In which the inter-relation between section 12 and section 2(24) has been brought out. Gifts made with clear directions that they shall form part of the corpus of the religious endowment can never be considered as income. In the case of R. B. Shreeram Religious & Charitable Trust v. CIT [1988] 172 ITR 373 (SC) it was held by the Bombay High Court that even ignoring the amendment to section 12, which means that even before the words appearing to parenthesis in the present section 12, it cannot be held that voluntary contributors specifically received towards the corpus of the trust may be brought to tax. The aforesaid decision was followed by the Bombay High Court in the case of CIT v. Trustees of Kasturbai Scindia Commission Trust[1991] 189 ITR 5 (Bom). The position after the amendment is a fortiori. In the present cases the Assessing Officer on evidence has accepted the facts that all the donations have been received towards the corpus of the endowments. In view of this clear finding, it is not possible to hold that they are to be assessed as income of the assessees. We, therefore, hold that the assessment of the corpus donations cannot be supported.'

1.5.5 The following decisions are also relevant:

1. *ITO v. Smt. Basanti Devi & Shri Chakhan Lal Garg Education Trust*, ITA No. 5082/Del./2010 date 19.1.2011, Delhi Tribunal.
2. *Director Income Tax v. Smt. Basanti Devi & Shri Chakhan Lal Garg Education Trust*, ITA No. 927/2009 date 23.9.2009, Delhi Tribunal.

In the light of the above case laws it is clear that corpus donation cannot be treated as income even if the trust is not registered under section 12AA or 12AA registration is cancelled.

Annexure 1

Text of Section 2(24) in the Income Tax Act, 1995

(24) " income" includes-

(i) profits and gains;

(ii) dividend;

(iia) voluntary contributions received by a trust created wholly or partly for charitable or religious purposes or by an institution established wholly or partly for such purposes 8 or by an association or institution referred to in clause (21) or clause (23), or by a fund or trust or institution referred to in subclause (iv) or sub- clause (v) of clause (23C) of section 10]. Explanation.- For the purposes of this sub- clause," trust" includes any other legal obligation;]

(iii) the value of any perquisite or profit in lieu of salary taxable under clauses (2) and (3) of section 17.

(iiia) 1 any special allowance 2 or benefit, other than perquisite included under sub-clause (iii), specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit;

(iiib) any allowance granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at a place where he ordinarily resides or to compensate him for the increased cost of living;]

(iv) the value of any benefit or perquisite, whether convertible into money or not, obtained from a company either by a director or by a person who has a substantial interest in the company, or by a relative of the director or such person, and any sum paid by any such company in respect of any obligation which, but for such payment, would have been payable by the director or other person aforesaid;

(iva) the value of any benefit or perquisite, whether convertible into money or not, obtained by any representative assessee mentioned in clause (iii) or clause (iv) of sub- section (1) of section 160 or by any person on whose behalf or for whose benefit any

income is receivable by the representative assessee (such person being hereafter in this sub- clause referred to as the" beneficiary") and any sum paid by the representative assessee in respect of any obligation which, but for such payment, would have been payable by the beneficiary;]

(v) any sum chargeable to income- tax under clauses (ii) and (iii) of section 28 or section 41 or section 59;

(va) 4 any sum chargeable to income- tax under clause (iiia) of section 28;]

(vb) any sum chargeable to income- tax under clause (iiib) of section 28; 6 (VC) any sum chargeable to income- tax under clause (iiic) of section 28;]

(vd) the value of any benefit or perquisite taxable under clause (iv) of section 28;

(ve) any sum chargeable to income- tax under clause (v) of section 28;]

(vi) any capital gains chargeable under section 45;

(vii) the profits and gains of any business of insurance carried on by a mutual insurance company or by a co- operative society, computed in accordance with section 44 or any surplus taken to be such profits and gains by virtue of provisions contained in the First Schedule;

(viii) Omitted by the Finance Act, 1988 , with effect from April, 1988 . It was inserted by the Finance Act, 1964 , w. e. f 1- 4- 1964 .]

(ix) any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever;]

(x) any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, 1948 (34 of 1948), or any other fund for the welfare of such employees;] interest in the company or a relative of the director or the other person. 4 The word' income' is of the widest amplitude and it must be given its natural and grammatical meaning. The definition of income in section 2 (24) is inclusive. The purpose of the definition is not to limit the meaning of' income' but to widen its net and the several clauses therein are not exhaustive of the meaning of income; even if a receipt did not fall within the ambit of any of those clauses, it might still be income if it partook the nature of income. The words" other games of any sort' were of wide

amplitude and their meaning was not confined to mere gambling or betting activities. Assuming that the expression" winnings" had acquired a particular meaning viz. receipts from activities of a gambling or betting nature only, it did not follow that monies received from non- gambling or non- betting activities were not included within the ambit of income. The assessee participated in a car rally and won a prize. The car rally was a contest, if not a race and the assessee entered the contest to win it. What he got was a return for his skill and endurance. It was" income" construed in its widest sense. Though it was casual in nature, it was nevertheless income.

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Published by **Dr. Sanjay Patra** on behalf of
FINANCIAL MANAGEMENT SERVICE FOUNDATION
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