



20th April, 2016

Mr. Arun Jaitley
Hon. Minister of Finance
Government of India
North Block
New Delhi - 110 001.

Respected Sir,

Sub : Addendum to Representation in respect of provisions relating to Direct Taxes of the Finance Bill, 2016

We refer to our Representation in respect of provisions relating to Direct Taxes of the Finance Bill, 2016 sent with our letter dated 6th April, 2016.

In this connection, we enclose herewith our further representation regarding new Chapter XII-EB proposed to be inserted by the Finance Bill, 2016 i.e. Special provisions relating to tax on accreted income of certain trusts and institutions.

We hope that our representation will receive due consideration. We will be pleased to present ourselves for any explanation and / or clarification that may be required by you.

Thanking you,

FOR BOMBAY CHARTERED ACCOUNTANTS' SOCIETY

Raman Jokhakar
President

Encl: As above.

Sanjeev Pandit
Chairman – Taxation Committee

Ameet Patel
Co-Chairman – Taxation Committee

CC:

- Shri Jayant Sinha, Minister of State for Finance
- Shri Ratan Watal, The Finance Secretary
- Dr. Hasmukh Adhia, The Revenue Secretary, Ministry of Finance
- Shri Atulesh Jindal, The Chairman, Central Board of Direct Taxes
- Member (Legislation & Computerisation), Central Board of Direct Taxes

BCAS – Addendum to the Post Budget Memorandum 2016

Special provisions relating to Tax on Accreted Income of Certain Trusts and Institutions – Chapter XII-EB – Sections 115 TD To 115 TF - Clause 60

The new Chapter XII-EB proposed to be inserted by the Finance Bill, 2016 provides for levy of tax on market value of assets of a charitable trust or institution under certain circumstances.

The Memorandum explaining the provisions of the Finance Bill, 2016 states that a society or a company or a trust or an institution carrying on charitable activity may voluntarily wind up its activities and dissolve or may also merge with any other charitable or non-charitable institution, or it may convert into a non-charitable organisation. In such a situation, the existing law does not provide any clarity as to how the assets of such a charitable institution shall be dealt with.

While appreciating the need for making provision for an 'exit tax' when a charitable entity ceases to be so, the provisions of the new Chapter are draconian and will cause extreme hardship in many cases, particularly those falling under the deeming fiction of sub-section (3) of the new section 115TD. These are enumerated below along with our suggestions.

(a) Section 2(15) defines 'charitable purpose'. This definition has been undergoing changes repeatedly. While an entity may continue to be a charitable entity, as is generally understood, due to change in the definition of the term 'charitable purpose' the entity may cease to be 'charitable' for the purposes of the Income-tax Act, 1961 (Act). There are a large number of entities which continue to be charitable and carry on their activities as charitable organisations, but due to the operation of the provisos to section 2(15), these entities may not be eligible for exemption u/s 11. These entities have not changed their activities and they continue to be charitable under the general law and have been using the corpus and the income for charitable purposes as was understood during the period when the corpus was built up. It is not fair and justified that such entities are levied tax on the market value of their assets.

Suggestion

It is therefore suggested that the deeming fictions of sub-section (3) should be deleted. Alternatively, mere cancellation of registration u/s 12AA of the Act should

not trigger the provisions of Chapter XII-EB. If an entity ceases to be a charitable entity for the purposes of the Act due to the operation of proviso to section 2(15), such an entity should not be charged tax on the market value of its assets as contemplated by Chapter XII-EB, so long as it continues to apply its corpus and income for charitable purposes as defined under section 2(15) without having regard to the provisos to the said section. Such an entity will, of course, pay tax at the rate applicable to an Association of Persons u/s 164(2) of the Act.

- (b) The new Chapter XII-EB proposes that the charitable entity will have to pay tax on the accreted income within 15 days from the date of cancellation of registration u/s 12AA of the Act.

It is the experience that cancellation of registration u/s 12AA of the Act has become rampant and common in recent times. Invariably the assessee - charitable entity - prefers an appeal and often the order cancelling the registration of the charitable entity is set aside and the registration is restored. In such circumstances, the proposed provision requiring such entity to pay tax under Chapter XII-EB within 15 days of the date of cancellation of registration will put the entity to extreme hardship and cause irreversible damage. In many case, this provision may even force the concerned entity to sell its assets to pay the tax on the accreted income and at a later date, in the appellate proceedings, the order of cancellation of registration may be set aside, and registration may be restored. However, by then, due to the operation of the provisions of the Chapter XII-EB, irreparable damage will have already been caused to the organisation.

Suggestion

Considering this, the levy of tax under Chapter XII-EB should be postponed till the order cancelling the registration becomes final, where such cancellation is the subject matter of an appeal.

- (c) Even in a case where tax on the accreted income is to be levied, a more reasonable period should be provided for. As mentioned above, to pay the tax on the accreted income, the entity may have to liquidate its investments, sell immovable property, etc. This takes considerable time. In fact, in States where law relating to charitable trusts

is in force, before selling an immovable property, a charitable trust requires to obtain the approval of the charity commissioner. This it takes several months.

Suggestion

Considering this, a period of six months may be permitted for payment of the tax on the accreted income.

- (d) Section 115TD(3) provides that when there is modification of objects of a charitable entity, and the modified objects do not confirm to the conditions of registration, and the entity has not applied for fresh registration u/s 12AA within the previous year or the application for the registration has been rejected, the entity will be deemed to have been converted into any form not eligible for registration u/s 12AA.

As mentioned in (a) above, so long as the objects of the trust conform to the definition of 'charitable purpose' as defined u/s 2(15) without having regard to the proviso thereto, the charitable entity should not be charged to tax on its accreted income.

Modification of objects may happen at the end of the previous year and in such a case it may be difficult to file an application for fresh registration within the previous year.

Suggestion

A reasonable period of one year should be permitted for the entity to make an application for registration u/s 12A/12AA. Even presently, section 12A provides a period of one year from the date of creation of the trust to make an application for registration.

Further, if the entity has filed an appeal against the order rejecting its application for registration u/s 12AA, the levy of tax should be postponed till the order rejecting the application for registration becomes final.

Presently, there is no provision in the Act for seeking fresh registration u/s 12A/12AA on modification of objects of the trust. In order to bring clarity, appropriate provisions may be made for seeking fresh registration u/s 12A/12AA on modification of objects of the trust.

- (e) The new Chapter provides that the principal officer, the trustee and the trust/institution shall be liable to pay the tax on the accreted income and in case of

failure to pay the tax they shall be deemed to be assesseees in default. As per the existing law, a trustee or the principal officer is liable only in his representative capacity. The new provision may be interpreted to mean that the trustee or the principal officer is personally liable for paying tax on the accreted income.

Suggestion

It should be clarified that the liability is only in the representative capacity and not in the personal capacity.

- (f) It is not clear how the provisions of the new Chapter will be implemented.

Suggestion

Appropriate provisions should be made for assessment, appeal and stay in the new Chapter.
