

**Implications arising from Amended Definition**  
**Of**  
**Charitable Purpose**



**VOLUNTARY ACTION NETWORK INDIA**  
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## **Implications arising from Amended Definition of Charitable Purpose**

### **1. Introduction:**

- 1.1 The amendment to the definition of “Charitable Purpose” arising from the amendment made through the budget of 2008 and effective from financial year commencing on 1<sup>st</sup> April 2008 and relating to assessment year 2009 – 10 is adversely affecting charitable intuitions.
- 2.1 The definition of ‘charitable purpose’ as now specified in section 2(15) of the Income tax Act 1961 is the following:

“**charitable purpose**” includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility:

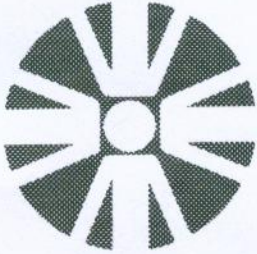
Provided that the advancement of any other object of general public utility shall not be charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess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

- 3.1 The Central Board of Direct Taxes issued Circular No. 11/2008 dated 19<sup>th</sup> December 2008 (copy attached as Annexure 1) addressing certain issues related to the amendment in the definition of ‘charitable purposes’. In this circular the following has been stated

“3.2. In the final analysis, however, whether the assessee has for its object ‘the advancement of any other object of general public utility’ is a question of fact. If such assessee is engaged in any activity in the nature of trade, commerce or business or renders any service in relation to trade, commerce or business, it would not be entitled to claim that its object is charitable purpose.”

2. **Implications:** Some of the difficulties arising from the above are the following:

- 2.1 **Adverse Impact on Multi Objective Charitable Institutions:** The above definition and circular dated 19<sup>th</sup> December 2008 places multi objective charitable institutions at a great disadvantage. If a charitable institution undertakes multi objectives i.e. education / medical activities / relief to the poor and also any other object of general



public utility and receives any fee, cess or other consideration towards the advancement of any other object of general public utility then it will lose its charitable status as an assessee. There are many such charitable institutions and they have been placed at a disadvantage, whereas the law protects the institutions undertaking educational, medical relief and relief to the poor activities. Hence these charitable institutions should be permitted to retain their charitable status and the activities relating to education, medical relief and relief to the poor and any activities related or incidental thereto should continue to be assessed as charitable institutions.

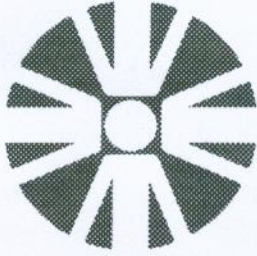
**2.2 Adverse Impact Where the Memorandum of Association has General Public Utility Objectives:**

A large number of charitable institutions have multifarious objectives and some of these objectives relate to undertaking publication of awareness creating material, which is sold, many a time at nominal rates or they make available audio / video CDs for a fee. Such organizations, though not actually undertaking the activity have it in their object clause and they would be adversely affected. These organizations would not be strictly within the confines of medical relief, education and relief to the poor and could lose the charitable status. The income tax department has always contested object clauses in matters relating to section 10(23C) and there is unnecessary litigation. Here again a large number of charitable institutions would be faced with litigation.

**2.3 Adverse Impact where the Government has Granted Approval for a Particular Purpose:**

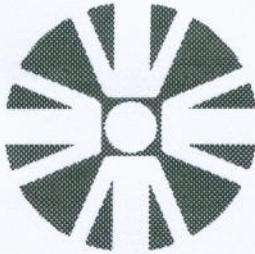
The government has allotted land and building to many charitable institutions to set-up and manage hostels for children, women in distress (need not be poor), working women or for community halls. In other cases charitable institutions have purchased land and building on their own to carry out these services. These institutions charge low hostel fees so as to manage the hostel and its maintenance. In such cases the charitable institution cannot change its objective because of the nature of its work, the allotment of land by the government and permission taken from local authorities e.g. municipal corporations for building use. Such institutions by charging a fee would lose the charitable purpose. They will have to pay taxes and also fringe benefit tax. The persons to lose in this situation would be the children, the women in distress and working women.

**2.4 Cancellation of 12A:** Where an organization has undertaken activities of general public utility and charged a fee or other consideration, then such activity would not be a charitable purpose. The next step by the income tax department would be to cancel the 12A registration u/s 12AA(3) of the Income tax Act 1961. The cancellation of the registration u/s 12A would imply that the institution would also have to pay fringe benefit tax, whereas the registration is canceled after the close of the financial year. In the next year when the institution ceases to undertake any



activity of general public utility for a fee it will have to once again seek registration u/s 12A, whereas this could be denied since in the previous year the income tax department has already taken an adverse stand and cancelled its 12A registration. This would put the charitable institution to undue hardship.

- 2.5 **No Opportunity Provided to Eschew Activities:** The Central Board of Direct Taxes vide Circular No. 11/2008 dated 19<sup>th</sup> December 2008 in paragraph 3.2 has stated that “Assessees, who claim that their object is ‘charitable purpose’ within the meaning of Section 2(15), would be well advised to eschew any activity which is in the nature of trade, commerce or business or the rendering of any service in relation to any trade, commerce or business.” However no opportunity has been granted to eschew such activities since the budget was passed in May 2008 and affects the financial year 2008 – 09 relevant to assessment year 2008 – 09. To eschew such activities needs some time and it cannot be undertaken overnight. If the definition to charitable purpose was to be changed in the manner that it has been done then for natural justice the charitable institutions should have been granted two to three years to make the change and eschew such activities. This has not been done and the charitable institutions have been placed at a great disadvantage having been hit below the belt overnight.
- 2.5 **Misuse by a Few is Resulting in Adversely Affecting the Charitable Organizations as A Whole:** The intention of the amendment to the definition of ‘charitable purpose’ is to exclude or deny the benefit of the charitable status to “purely commercially and business entities which wear the mask of charity.” The Income tax Act 1961 has section 12(3), which has granted power to the Commissioner to cancel the registration u/s 12A if the activities are not genuine or are not being carried out in accordance with the objects of the Trust or institution. Accordingly if there is misuse of the charitable purpose then the solution is to act u/s 12(3) and cancel registration u/s 12A. In this case the wrong doers would be penalized but by amending the definition of charitable purpose even genuine and bona fide charitable institutions doing good work are adversely affected just because they charge some fees or other consideration and undertake activities which are of a general public utility.
- 2.7 **Charitable Purpose and National Policy on the Voluntary Sector 2007:** The National Policy on the Voluntary Sector 2007 of the Government of India (copy attached as Annexure 2) inter-alia states the following:
- (i) **In Paragraph 1.1.- Preamble:** “This policy is a commitment to encourage, enable and empower an independent, creative and effective voluntary sector,



with diversity in form and function, so that it can contribute to the social, cultural and economic advancement of the people in India”.

- (ii) **Paragraph 3 – 3.1.– Objectives:** “To create an enabling environment for VOs that stimulates their enterprise and effectiveness and safeguards their autonomy.”
- (iii) **Paragraph 4.6 – Establishing an Enabling Environment of e the Voluntary Sector: .....** “The government will also simplify and streamline the system for granting income tax exemption status to charitable projects under the Income tax Act. At the same time, the Government will consider tightening administrative and penal provisions to ensure that incentives are not misused by paper charities for private financial gain.”
- (iv) **Paragraph 5.2 - Partnership in Development:** “Partnership between Government and VOs identifying shared goals and defining complementary roles. It must be based on the basic principles of mutual trust and respect, with shared responsibility and authority. These principles must be explicit in the terms and conditions of the partnership. They must also be evident in the formal and informal systems of collaboration.
- (v) **Paragraph 6.1 - Strengthening the Voluntary Sector:** “.....The government will support and encourage existing, as well new, independent philanthropic institutions and private foundations to provide financial assistance to deserving VOs. (voluntary organizations)”.

**2.7 Charitable purpose as Partner in Development:** The above National Policy shows that charitable purpose is partnership in development. The funds collected by charitable organizations are deployed for charitable purposes, which include objects of general public utility. Instead of paying income tax @ 30% to the Government, they deploy atleast 85% of the funds each year for charitable and development purposes. The charitable purpose with regard to general public utility is where the charitable organizations collect funds and do the work of the government. One of the objectives of taxation is to collect funds for development. The charitable organizations are fulfilling this role on behalf of the government e.g. addressing general public utility issues like environment, climate change, watershed management and if they collect fees from some of the stakeholders or beneficiaries then they loose their status as a charitable organization. Accordingly the Government should kindly withdraw the amendment undertaken to section 2(15) and instead penalize organizations that violate the principles of charitable purposes. If some



organizations wear a “mask” then it is not correct to penalize organizations that do not wear the mask but work for the good of the public.

3. **Conclusion:** In view of the above the difficulties being faced by genuine charitable organizations need to be addressed and that they should not be put to hardships and taken through litigation. In the absence of any grace period most of the charitable organizations are being adversely affected. The level of awareness amongst the charitable organizations about the change in the definition of “charitable purposes” is quite low at this stage and it would only be fair if first awareness is created for which a grace period of two to three years is required. It would be appropriate to penalize errant organizations that ‘wear the mask’ rather than all charitable organizations, which render services by raising resources on their own. In charging some fees or consideration the persons or stakeholders making the payment derive a stake or self satisfaction in the development work or are able to access facilities at very nominal charges, which would otherwise be difficult to access.