Social Sector Hotline

February 13, 2023

SOCIAL SECTOR BULLETIN: MONTHLY UPDATE

BACKGROUND

- Proposal for an Entity DigiLocker to be set up to store information for use by MSMEs, large business and charitable trusts;
- Proposal to set up an Agriculture Accelerator Fund to encourage agristartups by entrepreneurs in rural areas
- A Green Credit Programme to encourage enterprises, individuals, and local governments to take ecologically sustainable and responsive actions;
- Trust cannot claim exemptions under foreign charitable grants if not registered under Section 12 of the Income Tax Act, 1961;
- Belated opening of FCRA account and filing of FC-4 cannot be condoned where no foreign funds were received until the opening of the FCRA account.

BUDGET 2023: UPDATES IN THE SOCIAL SECTOR

The Indian Finance Minister, Nirmala Sitharaman, presented the Union Budget ("**Budget**")[2] of India for the financial year 2023-24 on February 1, 2023. The budget encompasses seven focus areas for 2023-2024 – inclusive development, reaching the last mile, infrastructure and investment, unleashing the potential, green growth, youth power and financial sector.

The government has introduced key changes in the tax regime while also proposing innovation in financing in different sectors across the economy. There have been key proposals introduced for the not-for-profit sector to collaborate blended finance with social sector finance. This is a welcome change given the recent in-principal nod by Securities Exchange Board of India ("**SEBI**") for setting up a Social Stock Exchange ("SSE") as an alternative means of funding for not-for-profits.

The Finance Minister has announced for an Entity DigiLocker to be set up for MSMEs, large business and charitable trusts. The DigiLocker will store and share documents with authorities, regulators, banks and other business entities through a secure online mechanism. This would help in better regulating the not-for-profit sector. The DigiLocker would ensure proper handling and availability of data for efficient transacting in the sector.

Input Tax Credit for Corporate Social Responsibility("**CSR**") related expenditures Section 17(5) of the Central Goods and Services Tax ("**CGST**") Act[3] is proposed to be amended ensuring that input tax credit is not available for goods or services received by a taxable person and used or intended to be used for activities related to their obligations under CSR as defined in Section 135 of the Companies Act, 2013.[4] The proposed change will bring in much sought after clarity in this sphere for better compliance by companies.

The 2023 budget includes proposed amendments relating to exemption provided to charitable trusts and institutions. It shall provide clarity on tax treatment on replenishment of corpus and on repayment of loans/borrowings. The amendments aim at treating only 85 per cent of donation made to other trusts as application and omitting redundant provisions related to rolling back of exemption. The government shall combine provisional and regular registration in some cases, modify the scope of specified violation and align of time for furnishing of certain forms. If a trust does not apply for exemption after getting provisional exemption they shall be provided for payment of tax on assets and for reexemption after expiry of exemption. However, the time provided for furnishing return of income for claiming exemption shall not include the time provided for furnishing updated return.

The government has also proposed for an Agriculture Accelerator Fund to be set-up to encourage agristartups by entrepreneurs in rural areas. The Fund will aim at bringing modern technologies to transform agricultural practices, increase productivity and profitability in rural India. The fund would allow for innovation for low-cost products to better equip the agriculture sector with modern technology.

To support the above proposal, a Green Credit Programme will be notified under the Environment (Protection) Act to encourage behavioural change. This will encourage enterprises, individuals, and local governments to take ecologically sustainable and responsive actions, as well as assist mobilise more resources for such initiatives. Such joint efforts would allow for a social, technological and knowledge-driven change in the agriculture sector whilst promoting entrepreneurship in rural India. Moreover, CSR funding in such schemes would better allow for companies to reach their ESG goals while supporting governmental efforts in green financing.

The budget has proposed for several innovative schemes and mechanisms to integrate a technology driven growth

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in the economy. Inclusion of blended financing and collaborative approach towards financial sector growth and social sector financing would allow the Indian economy to compete with other emerging economies, globally.

TRUST CANNOT CLAIM EXEMPTIONS UNDER FOREIGN CHARITABLE GRANTS IF NOT REGISTERED UNDER SECTION 12 OF THE INCOME TAX ACT, 1961 ("ITA")

The Foreign Contribution Regulation Act ("**FCRA**") acts as a watchdog for foreign grants routed to Indian not-for-profits. Foreign contributions or hospitality received by individuals or not-for-profits are subject to FCRA regulation. It restricts receiving and utilizing foreign contributions for any conduct or incidental acts that are against the interests of the country. The Act also applies to corporations that are registered or incorporated in India but have branches or subsidiaries outside of India.

Recent judgements in this sphere for the month of January 2023 aid us in navigating through intricate provisions of laws impacting the foreign funds received by a not-for-profit and taxes levied thereof. We will now walk through these judgements:

In **Akshay Educational & Social Welfare Charitable Trust v. Deputy Commissioner of Income-tax**[5], the Court held that a trust cannot claim exemptions under foreign charitable grants if the said trust is not registered under Section 12 of the Income Tax Act, 1961 ("**ITA**")

Per the facts of the case, the aim and objective of the assessee trust was to work towards causes prevailing in the weaker sections of the society. In the relevant assessment year, the assessee claimed foreign contribution received for specific infrastructural development as a 'capital receipt' not taxable albeit the lack of proper registration under Section 12 of ITA. The trustees in consultation with the chairman can use the said fund for trust activities, if required. Thus, it cannot be deemed as a donation towards corpus fund.

The Court dismissed the appeal on the following grounds:

- Per Section 2(24)(iia) ITA, 'income' shall also encompass voluntary contributions obtained with a definite directive that they form part of the corpus of the trust. Hence, liable to be included in the assessee's income.
- All types of voluntary contributions received by a trust established entirely or partially for charity or religious purposes, or an institution founded fully or partly for such reasons, are included in the trust's income.
- Per section 11(1)(d), any voluntary contribution received by a trust following a specific direction for such contribution as part of the corpus shall be invested or deposited per the prescribed modes maintained specifically for the said corpus fund shall not be treated as income but capital contribution.
- However, the above criteria is subject to section12A, i.e., for any exemption claim, the assessee should be registered with the Income Tax Department under section 12A.

While corpus contributions are recognised as income in the hands of the beneficiary trust, if such trust meets the conditions of exemptions under sections 11 and 12 and is registered under section 12A, such corpus donations are excluded from their income. However, if such trust is not eligible for exemption under section 11, either because it does not meet the requirements set out in section 12A or because it falls within section 13, corpus contribution will be included in such trust or institution's income.

BELATED OPENING OF FCRA ACCOUNT AND BELATED FILING OF FC-4 CANNOT BE CONDONED WHERE THE NOT-FOR-PROFIT DID NOT RECEIVE FOREIGN FUNDS UNTIL THE OPENING OF THE FCRA ACCOUNT

In **WNS Cares Foundation v. Union of India**[6] , the court held that belated opening of FCRA account and belated filing of FC-4 cannot be condoned where the not-for-profit did not receive foreign funds until the opening of the FCRA account

- Form FC-4 states that the receipt of foreign contributions must be given "as of 31st March of the year ending," and the bank account must be at the SBI, Sansad Marg branch. The court saw merit in the case since the Petitioner not-for-profit created its account in August 2021, and the Foreign Contribution Regulation (Amendment) Act, 2020 had not been enforced as on March 31, 2020.
- The court allowed the Petitioner to file the details of its FCRA account in serial no.7 of the Form FC – 4. The court further directed for no coercive steps to be taken against the Petitioners for delayed opening of the FCRA account since no foreign contribution was received by them in the FY 2019-2020 and FY 2020-21. Therefore, no penalty was imposed upon the Petitioners if the returns for FY 2019-2020 and FY 2020-21 are filed within a period of one month.

It is imperative for Indian not-for-profits and the foreign funders alike to be aware of FCRA's requirements and ensure compliance of the same. Additionally, any use or transfer of such funds must be meticulously evaluated and coordinated. Philanthropic organisations that are FCRA registered must make sure that they are in compliance with the rules and that the accompanying documentation is maintained and current at all times. Before being accepted by the registered organizations, all incoming contributions and their objectives must also be thoroughly examined in light of FCRA.

– Rahul Rishi

You can direct your queries or comments to the authors

[1]Rahul Rishi (The author would like to acknowledge and thank Ms. Shhreiya Agarawal (intern) for her contribution to this hotline.)

[2]https://www.indiabudget.gov.in/doc/budget_speech.pdf

[3]https://www.cbic.gov.in/resources//htdocs-cbec/gst/cgst-act.pdf

[4]https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf

September 26, 2024

Scope of judicial interference and inquiry in an application for appointment of arbitrator under the (Indian) Arbitration and Conciliation Act, 1996

September 22, 2024

[5]Akshay Educational & Social Welfare Charitable Trust v. Deputy Commissioner of Income-tax [2023] 146 taxmann.com 529 (Patna - Trib.).

[6]WNS Cares Foundation v. Union of India [2023] 146 taxmann.com 386 (Delhi).