INTERface

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Financial Management Service Foundation
• Promoting Accountability •
fmsf

HIGHLIGHTS

- Landmark ruling by supreme court regarding set off of past deficit
- Budget 2018 – FCRA retrospective amendment
- Notional expenditure in development projects
- Tax impact under various types of CSR activities

The Answer is in your hands

There was once a wise woman who lived by herself near a small village. Rumor had it that she could always accurately predict when the rains would come, or help heal a sick child with herbs, or calm angry neighbors and help them to resolve their fights and arguments. People came from all over the land to meet with her and seek her advice on matters both small and great. Her reputation was such that it was said she was never wrong — not even once.

Some of the children of the village didn't believe that it was possible to always be right. Surely she could not know everything! They decided to test her knowledge. First they asked her to answer questions about the planets, the animals, and the world. No matter how hard the questions, she always answered correctly.

The children were amazed at her knowledge and learning and most were ready to stop testing the wise woman. However, one boy was determined to prove that the old woman couldn't know everything. Hatching a devious scheme, he told all of his friends to meet him at the woman's home the following afternoon so he could prove her wrong.

All through the next day he hunted for a bird. Finally he caught a small bird in a net. Holding it behind his back so no one could see what was in his hands, he walked to the wise woman's home.

The woman walked calmly to the door. "May I help you?" she simply asked.

"You say you know everything — prove it — what am I holding behind my back?" the young boy demanded.

The old woman thought for a moment. She could make out the faint sounds of a bird's wings rustling. "I do not say I know everything — for that would be impossible," she replied. "However, I do believe you are holding a bird in your hands."

The boy was furious. How could the woman have possibly known he had a bird? Thinking quickly, he came up with a new scheme. He would ask the woman whether the bird was alive or dead. If the woman replied, "alive," he would crush it with his hands and prove her wrong.

If she answered, "dead," on the other hand, he would pull the living bird from behind his back and allow it to fly away. Either way he would prove his point and the wise woman would be discredited.

"Very good," he called. "It is a bird. But tell me, is the bird I am holding alive or dead?"

Again the woman spoke calmly, "The answer, my young friend, is in your hands. The answer is in your hands."

The boy realized that the wise woman had once again spoken correctly and truthfully. The answer was indeed in his own hands. Feeling the bird feebly moving in his hands as it tried to escape his grasp, he felt suddenly very ashamed.

The answer was in his hands — slowly and gently he brought his hands to the front of his body. Looking into the eyes of the delicate bird he apologized, "I am sorry little one," and he opened his hands to let her go free.

Many times, the answer is indeed in our hands but without trying we look at options outside of us. A lot can be achieved if we make efforts in the right earnest to be part of the answer than posing the problem!

Sanjay Patra

Acknowledgement

We are grateful to the authors who have contributed for the articles in this edition.

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I. LEGAL

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INTEGRATION OF BANK ACCOUNTS WITH PFMS UNDER FCRA

1. INTRODUCTION

1.1 The Ministry of Home Affairs, Foreigners Division has issued a notification No. 2/21022/58(951)/2017/FCRA(MU), regarding integration of bank accounts under FCRA 2010 with PFMS. The copy of the notification is provided in Annexure 1.

1.2 Under PFMS, the banks are required to integrate their system with the Government PFMS, which will enable the FCRA Department to track transactions online.

1.3 As per the notification, only 32 banks in the country have integrated their systems with PFMS. Therefore, the FCRA Department has directed all the FC registered organisations to shift their bank accounts to one of the 32 notified banks. The list of notified banks is provided in Annexure 2.

1.4 The organisations, which are already having their account in one of these 32 banks, are not required to do anything in this regard.

1.5 All other organisations should change their bank accounts to one of the 32 notified banks. It may be noted that this notification applies to both designated bank account and multiple bank accounts.

1.6 This exercise shall be completed expeditiously within one month of the publication of this notice with intimation of the details of the bank accounts so opened in the prescribed format as provided under Rules 9 and 17A of Foreign Contribution (Regulation) Rules, 2011.

1.7 The organisations who have received prior permission are also required to change the bank account as per the notification.

1.8 Multiple bank accounts are also required to be shifted. In this context, it has been noticed that the FCRA Department website does not allow multiple uploading of Form FC 6 simultaneously. For such cases the way forward has also been discussed here in this issue.

2. WHAT IS PFMS

2.1 The Public Financial Management System (PFMS), earlier known as Central Plan Schemes Monitoring System (CPSMS), is a web-based online software application developed and implemented by the Office of Controller General of Accounts (CGA). PFMS was initially started during 2009 as a Central Sector Scheme of Planning Commission with the objective of tracking funds released under all Plan schemes of GoI, and real time reporting of expenditure at all levels of Programme implementation. Subsequently in the year 2013, the scope was enlarged to cover direct payment to beneficiaries under both Plan and non-Plan Schemes. The latest enhancement in the functionalities of PFMS commenced in late 2014, wherein it has been envisaged that digitization of accounts shall be achieved through PFMS and the additional functionalities would be built into PFMS in different stages. Beginning with Pay & Accounts Offices payments, the O/o CGA did further value addition by proposing to bring in more financial activities of the Government of India in the ambit of the project.

2.2 The primary objective of PFMS is to facilitate sound Public Financial Management System for Government of India (GoI) by establishing an efficient fund flow system as well as a payment cum accounting network. PFMS provides various stakeholders with a real time, reliable and meaningful management information system and an effective decision support system, as part of the Digital India initiative of GoI.

2.3 The enhanced application is envisaged to cater to all Plan and Non Plan payments of GoI, all tax and non-Tax receipts and also functions such as a comprehensive HRMIS and self-contained pension as well as GPF modules. Futuristically, all the existing standalone systems currently catering to various functions in Government of India will be subsumed in PFMS.

2.4 The biggest strength of PFMS is its integration with the Core banking system in the Country. As a result, PFMS has the unique capability to push online payments to almost every beneficiary/vendor. At present, PFMS interface is having interface in addition to the Core Banking System (CBS) of all Public Sector Banks, Regional Rural Banks, major private sector banks, Reserve Bank of India, India post and Cooperative Banks.

3. PROCEDURE FOR CHANGE OF BANK ACCOUNT

3.1 When a change of bank account becomes a necessity, the following procedure may be followed:

- A new bank account, which is proposed to be designated bank account, should be opened by depositing the minimum amount required for opening of the account.
- The new rule allows change of designated Bank Account. It may be noted that earlier, for change in designated Bank Account, prior approval of the FCRA Department was necessary.
- Now onwards such change can be made without permission and only an intimation is required to be filed electronically online in Form FC 6 within 15 days of such change.
- The change in bank account should be accompanied by the Resolution of Governing Body for proposed change of Bank/Bank Account. A model format of the minutes along with the resolution for change of bank account is provided in Annexure 3. This resolution is not required to be reported.
- It is not legally necessary to close the old account. Therefore, the organisation may use the old account as a domestic account. But it is desirable to close the old account, to ensure that even by mistake the foreign funds are not credited to the old account.

3.2 The Rules of 17A as Amended by Foreign Contribution Regulation Rule, 2015 published vide Notification No. GSR (E) dated the 14th December, 2015.

*****17A. Change of designated bank account, name, address, aims, objectives or Key members of the association:-***

A person who has been granted a certificate of registration or prior permission under section 11 of the Act shall intimate electronically online in Form FC-6, within fifteen days, of any change in the following, namely:-

- name of the association or its address within the State for which registration/ prior permission has been granted under the Act;

- its nature, aims and objects and registration with local/relevant authorities.;
- bank and/or branch of the bank and/or designated foreign contribution account number; and
- key members of the association if at any point of time such change causes replacement of fifty percent or more of the original key members as reported in the application for grant of registration/ prior permission/ renewal of registration under the Act.";

4. DO WE NEED TO CHANGE THE MULTIPLE BANK ACCOUNT ALSO

4.1 Under FCRA 2010 organisations are permitted to open multiple bank account for utilisation purposes, in addition to the primary designated bank account. After this notification all bank accounts including the multiple bank account should be shifted to a PFMS integrated bank as per the list provided in Annexure 2.

5. IS IT PRACTICALLY POSSIBLE TO SHIFT MANY MULTIPLE BANK ACCOUNTS AND FILE FORM FC 6 FOR EACH ONE OF THEM

5.1 It is practically very difficult to shift many multiple bank accounts and file Form FC 6 for each one of them. It has been noticed that the FCRA website does not permit multiple uploading of Form FC 6 regarding change in bank account.

6. WAY FORWARD

6.1 It is suggested that the following way forward may be adopted:

- The designated FC bank account should be changed and shifted as per the procedure prescribed.
- All the multiple bank account can be closed by transferring the balance to the existing designated bank account.
- New multiple bank accounts may be opened as per need in the PFMS integrated bank. Further, intimation regarding such new bank account may be sent to FCRA Department. In case the website does not allow filing of multiple Form FC 6 for such bank accounts, then the organisation may continue operating the new bank accounts and also contact for support from FCRA Department at the following number and email:

  FCRA Support center: 011-23077505
  Eamil: support-fcra@gov.in

Annexure-1

NO. 2/21022/58(951)/2017/FCRA(MU)
GOVERNMENT OF INDIA
MINISTRY OF HOME AFFAIRS
(FOREIGNERS DIVISION)
Major Dhyan Chand National Stadium
Outer India Gate, New Delhi-110001

Dated: 21.12.2017

NOTICE

Subject: Integration of Bank Accounts (of individuals/organisations who receive foreign contributions under the FCRA, 2010) with the PFMS

1. Whereas Foreign Contribution (Regulation) Act, 2010 (FCRA, 2010) provides for the regulation of acceptance of the foreign contribution (FC) or foreign hospitality by certain individuals/associations/organisations/companies to ensure that such contributions or hospitality is not being utilised for the activities detrimental to the national interests and matters connected therewith or incidental thereto. Under the powers conferred by the Act, Central Government has decided that all banks where the FCRA registered persons/organisations have opened their FC accounts would be integrated with Public Financial Management System (PFMS) for providing a higher level of transparency and hassle free reporting compliance.

2. Whereas, some banks have already integrated their systems with the PFMS for the above purpose.

3. Whereas, many banks have still not completed the above integration of their systems with the PFMS despite repeated letters, directions and meetings.

4. Therefore, in exercise of the powers conferred under section 46 of the FCRA, 2010, the Central Government hereby directs all persons who are either registered or who have sought prior permission under the FCRA, 2010 shall open their bank accounts as mandated in section 17 of the FCRA, 2010 in one or more of the banks in the enclosed list. This exercise shall be completed expeditiously within one month of the publication of this notice with intimation of the details of the bank accounts so opened in the prescribed format as provided under Rules 9 and 17A of Foreign Contribution (Regulation) Rules, 2011.

Sd/-
(Ravinder Kumar)
Director (MU)
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Annexure-2

S.NO.	NAME OF BANK
1	Abu Dhabi Commercial Bank
2.	ICICI Bank
3.	The Cosmos Co-Operative Bank
4.	Bank of Baroda
5.	State Bank of India
6.	South Indian Bank
7.	IDBI Bank
8.	Central Bank of India
9.	Corporation Bank
10.	Karur Vysya Bank
11.	Tamilnad Mercantile Bank Ltd.
12.	The Catholic Syrian Bank Ltd.
13.	HDFC Bank Ltd.
14.	UCO Bank
15.	IndusInd Bank Limited
16.	City Union Bank
17.	Syndicate Bank
18.	Allahabad Bank
19.	The Jammu and Kashmir Bank Ltd.
20.	Punjab National Bank
21.	Allahabad UP Gramin Bank
22.	DCB Bank Ltd.
23.	Manipur State Co-op Bank
24.	Vijaya Bank
25.	Bombay Mercantile Co-operative Bank Ltd.
26.	Yes Bank
27.	Oriental Bank of Commerce
28.	Dena Bank
29.	Bank of Maharashtra
30.	Canara Bank
31.	Andhra Bank
32.	Axis Bank

Annexure-3

MODEL FORMAT OF MINUTES REGARDING CHANGE IN BANK ACCOUNT & RESOLUTION

Minutes of the meeting of the members of ".. organisation" held on ...., 20 ....

A meeting of the board of m embers of "... Organisation" was held on ...., 20 .... at .... a.m./p.m. in the Registered Office at ....

Members present:

i. ……………………….

ii. ……………………….

iii. ……………………….

iv. ……………………….

v. ……………………….

1) Mr./Mrs/Ms. .... was voted to the chair.

2) **Leave of absence :**

Letters from Mr./Mrs./Ms. .... and Mr./Mrs./Ms. .... regretting their inability to attend the meeting was placed on the table and leave of absence was granted.

3) **Confirmation of the minutes of the previous meeting :**

The minutes of the meeting held on ...., 20 .... were read and confirmed.

4) **Change of Designated FCRA Bank Account :**

The governing body member, Mr./Mrs./Ms. .... proposed that for administrative convenience or other reasons ...., a new savings/current account be opened with .... bank at .... The proposal was seconded by Mr./ Mrs./Ms. .... and passed unanimously. It was further proposed that all the necessary legal compliances under FCRA, 2010 and other statutes be made as per the legal requirements.

Accordingly, the following resolution was passed:

"RESOLVED that a new savings/current account be opened in the name of ...." with .... bank, ... branch.

FURTHER RESOLVED that Mr./Mrs./Ms. ...., Mr/ Mrs./Ms. ....and Mr./Mrs./Ms. .... be the authorised signatories and the account may be operated by any two of the authorised signatories jointly".

5) **Other issues, if any :**

....

The meeting terminated with a vote of thanks to the chair

(Chairman)

BUDGET 2018 – FCRA RETROSPECTIVE AMENDMENT

1. SUMMARY

1.1 The Finance Bill 2018 has amended the definition of foreign source retrospectively with effect from 5th August, 1976 the date of commencement of the Foreign Contribution (Regulation) Act, 1976. This amendment is primarily intended to protect political and other institutions which received donation from subsidiaries of foreign companies in violation of FCRA.

1.2 The FCRA 1976 had provision which deemed Indian companies as foreign source if more than 50% shareholding was held by foreigners. As a result any donation received from such company was also treated as foreign contribution.

1.3 Under FCRA 1976 it was permissible for a organization of political nature to receive foreign funds subject to prior approval. There have been litigations against money political and other institutions regarding receipt of donation from subsidiaries of foreign companies. The Delhi High Court in the case Association for Democratic Reforms(ADR) vs Union of India, W.P.(C) 131/2013, judgement dated 28th March, 2014 ruled that FCRA law had been violated.

1.4 The Finance Act 2016 amended the FCRA Act retrospectively from 2010 and change the definition of "foreign source" as a result the donations received from such companies was no longer considered as foreign contribution. However the FCRA violations in the impugned cases pertained to period prior to 2010, therefore there was a need to extend the effect of the amendments way back to 1976.

1.5 The Budget 2018 has further extended the retrospective effect to 1976 and thereby all donation received by all recipients from foreign subsidiaries becomes local contributions. It may be noted that it is permissible for a political institution to receive donation from a Indian company but it cannot receive contribution from foreign source.

2. LANDMARK DECISION OF DELHI HIGH COURT

2.1 In the case Association for Democratic Reforms (ADR) vs Union of India, judgement dated 28th March, 2014 the Delhi High Court held major National political parties BJP and Congress were guilty of taking foreign funding and violating the provisions of FCRA and directed the Ministry of Home Affairs (MHA) and Election Commission of India (ECI) to take action against the two parties within six months. It was observed by the Court that these political parties had taken donations from Vedanta & its subsidiaries, registered in England and Wales, and its subsidiaries. The Bench also rejected the stand taken by Ministry of Home Affairs, which said that FCRA has not been violated. The judgment drew attention to the donations made to INC and BJP for the period up to the year 2009.

2.2 As a response to the above judgement the Finance Act 2016 amended the FCRA Law with retrospective effect. However the amendment to FCRA 2010 did not help the recipient of foreign contribution from such companies prior to 2010. Therefore this year the Finance Bill 2018 as proposed to extent the effect of amendments to 5th August 1976 retrospectively.

3. THE PROPOSED AMENDMENTS

3.1 The Finance Bill 2018 has amended the FCRA 1976 w.e.f from 5th August, 1976. It is ironical that an amendment has been made to an act, which has been repealed since September 2010.

3.2 In fact the Finance Act 2016 had amended the sub-clause (vi) of clause (j) of subsection (1) of section 2 of the Foreign Contribution (Regulation) Act, 2010. By virtue of this amendment all contributions made by Indian Companies with foreign shareholding in excess of 50% were excluded form the definition of foreign source. It may be noted that prior to this amendment all Indian Companies with more than 50% shareholding by foreigners were treated as foreign source and FCRA law was applicable. Ironically, under this law Indian companies like ICICI Bank or Infosys were not entitled to give donations even to their own foundations without FCRA prior permission or registration. The proposed amendment is as under:

"These amendments will take effect from 1st April, 2018.

Clause 217 of the Bill seeks to amend section 236 of the Finance Act, 2016 which relates to amendment to sub-clause (vi) of clause (j) of sub-section (1) of section 2 of the Foreign Contribution (Regulation) Act, 2010. The proviso to the said sub-clause inserted under the Finance Act, 2016 states that notwithstanding the nominal value of share capital of a company exceeding one-half per cent. at the time of making contribution, such company shall not be deemed to be a foreign source, if the foreign investment is within the limit specified under the Foreign Exchange Management Act, 1999 or the rules or regulations made thereunder. It is proposed to bring the said amendment with effect from the 5th August, 1976 the date of commencement of the Foreign Contribution (Regulation) Act, 1976, which was repealed and re-enacted as the Foreign Contribution (Regulation) Act, 2010."

4. MEANING OF 'FOREIGN SOURCE' UNDER FCRA

4.1 Unlike the term 'foreign contribution' which has been defined specifically, the term 'foreign source' is given only an inclusive definition in FCRA. The statutory definition of 'foreign source' as per section 2(1)(j) of FCRA, 2010 after incorporating the amended proviso is as follows :

(j) "foreign source" includes, —

- the Government of any foreign country or territory and any agency of such Government;
- any international agency, not being the United Nations or any of its specialised agencies, the World Bank, International Monetary Fund or such other agency as the Central Government may, by notification, specify in this behalf;
- a foreign company;
- a corporation, not being a foreign company, incorporated in a foreign country or territory;
- a multi-national corporation referred to in sub-clause (iv) of clause (g);
- a company within the meaning of the Companies Act, 1956, and more than

one-half of the nominal value of its share capital is held, either singly or in the aggregate, by one or more of the following, namely:—

A. the Government of a foreign country or territory;

B. the citizens of a foreign country or territory;

C. corporations incorporated in a foreign country or territory;

D. trusts, societies or other associations of individuals (whether incorporated or not), formed or registered in a foreign country or territory;

E. foreign company;

"Provided that where the nominal value of share capital is within the limits specified for foreign investment under the Foreign Exchange Management Act, 1999, or the rules or regulations made there under, then, notwithstanding the nominal value of share capital of a company being more than one-half of such value at the time of making the contribution, such company shall not be a foreign source;".

– a trade union in any foreign country or territory, whether or not registered in such foreign country or territory;

– a foreign trust or a foreign foundation, by whatever name called, or such trust or foundation mainly financed by a foreign country or territory;

– a society, club or other association of individuals formed or registered outside India;

– a citizen of a foreign country."

4.2 As is evident, the term "foreign source" has not been defined exhaustively. The Act has given an inclusive definition of the term 'foreign source' and that includes the sources mentioned in clauses (i) to (x). It may be noted that under clause (vi) above, a foreign source includes an Indian company if more than 50% of its share capital is held by persons covered under foreign source. However, by virtue of Finance Bill 2016 this clause shall not be applicable to those companies whose foreign shareholding is within the limits specified for foreign investment under the Foreign Exchange Management Act, 1999.

5. CONCLUDING REMARK

5.1 This amendment is apparently an attempt to protect various powerful institutions, which had violated FCRA laws. It is unfortunate that the law makers themselves fiddle with the law to protect specific interest. In this case the retrospective effect has been extended to 1976, which is unusual and a subject matter of debate whether such amendments are constitutionally permissible. What about those institutions, which may have been penalised for these violations in last 40 years.

5.2 Having said that, on flip side it is a much-needed correction of an anomaly which was existing by mistake in the FCRA Act. The Act when it was amended in 2010 consciously changed the definition of a foreign company with the intent to exclude all Indian companies with more than 50% foreign shareholding. It may be noted that in the FCRA Act 1976 the definition of a foreign company included all Indian companies with more than 50% foreign shareholding.

5.3 However, probably by oversight the definition of foreign source was not amended and due to such partial amendment, the FCRA law technically continued to apply to all Indian companies with more than 50% foreign shareholding.

5.4 Barring the political conflict of interest, it is a positive change and it will provide an opportunity to all charitable organizations (including those without FC registration) to access corporate grants and CSR funds. Many of the larger corporates of India have more than 50% foreign shareholding and they were compelled to work with

FC registration organizations only. FC registered organizations constitute a small portion of the NPOs sector, therefore this amendment will promote wider and greater reach of corporate grants to NPOs.

BUDGET 2018 - BUSINESS PROVISIONS APPLIED TO NGOs

1. SUMMARY

1.1 The Finance Bill 2018 has made radical changes with regard to computation of application/expenditures of NGOs. Amendments have been made to section 10(23C) and section 11 in order to apply the provisions of section 40(a)(ia) and 40A(3).

1.2 Now onwards, while computing amount of application subject to Sec. 11 section 10(23)(C), the following amount shall not be considered as application:

- If any payment is made in excess of Rs.10,000/- other than by way of A/c Payee cheque or A/c payee bank draft or use of Electronic Clearing System through a bank account or
- If any application of income is claimed on the basis of provision as liability and subsequently the liability in excess of Rs 10000/- is discharged other than by paying by way of A/c Payee cheque or A/c payee bank draft or use of Electronic Clearing System through a bank account.
- If the payments are subject to TDS provision and if TDS is not deducted thereon, then 30% of such sum payable shall not be considered as application. However the same amount shall be considered as application in the year in which the corresponding tax is deducted & deposited with the Govt.

1.3 These changes reflect a paradigm shift in the taxation and assessment of NGOs as provisions under the head “Business and Profession” will apply to the assessment of Trust and NGOs. It may be noted that under the current scheme of the Income Tax Act, Trust and NGOs are not assessed under five head of income and section 14 which provides for computation under five heads of income does not apply to them.

2. PROPOSED AMENDMENT IN DETAIL

2.1 The Finance Minister in his budget speech has said that at present, there are no restrictions on payments made in cash by charitable or religious trusts or institutions. There are also no checks on whether such trusts or institutions follow the provisions of deduction of tax at source under Chapter XVII-B of the Act. This has led to lack of an audit trail for verification of application of income.

2.2 Hence in order to encourage the less cash economy and reduce the generation and circulation of black money, it is proposed to insert a new Explanation to the section 11 to provide that for the purposes of determining the application of income under the provisions of sub-section (1) of the said section, the provisions of sub-clause (ia) of clause (a) of section 40, and of sub-sections (3) and (3A) of section 40A, shall, mutatis mutandis, apply as they apply in computing the income chargeable under the head “Profits and gains of business or profession”.

2.3 It is also proposed to insert a similar proviso in clause (23C) of section 10 so as to provide similar restriction as above on the entities exempt under sub-clauses (iv), (v), (vi) or (via) of said clause in respect of application of income. These amendments will take effect from 1st April, 2019 and will, accordingly, apply in relation to the assessment year 2019-20 and subsequent years.

3. PENALISING EXPENDITURE MADE IN CASH ABOVE RS. 10,000/-

3.1 The Finance Act 2018 has linked Section 40A(3) with the Trust and NGOs. Section 40A(3) is about the requirement of payment of any expenditure exceeding Rs.10,000/- in a day by A/c Payee cheque or use of Electronic Clearing System through a bank account.

3.2 Similarly Sec. 40A(3A) provides that whenever expenditures claimed on the basis of a liability then subsequently such liability is also required to be paid by A/c Payee cheque or A/c payee bank draft or use of Electronic Clearing System through a bank account provided a payment in a day exceeds Rs.10,000/-.

3.3 However, both the sections also provides that no disallowance shall be made and no payment shall be deemed to be the profits and gains of business or profession if such payment is justified based on circumstances, nature and extent of the banking facility available and other relevant factors. With regard to NGOs the following implications are foreseen:

– All cash payment exceeding Rs. 10,000/- shall not form part of Application of Income.

– Where an expenditure is claimed as Application on the basis of liability, then such liability which exceeds Rs. 10,000/- in a day should not be paid in cash otherwise it will be disallowed.

– Firstly, any disallowance a subject to the facts and circumstances under which cash payments were made under Rule 6DD of the Income Tax Rules, 1962.

– Secondly, any disallowance would not imply that such disallowance will result in increase in taxable income. Because unlike business entities for NGOs any disallowance does not result in taxable income. Therefore, even after disallowance the NGOs income will not become taxable unless the total unspent income including such disallowance exceeds 15% of total income. It may be noted that trusts and NGOs are required to apply 85% of the total income during the year.

4. IF TDS IS NOT DEDUCTED SECTION 40(A)(IA)WILL APPLY

4.1 Section 40(a)(ia) provides that 30% of any sum payable should be disallowed on which TDS should have been deducted and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in subsection (1) of section 139.

4.2 The law allows deduction if tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, thirty per cent of such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid. In other word the 30% disallowance can be claimed in subsequently.

4.3 NGO makes various payments which are subject to TDS provisions and therefore NGO should deduct Tax and deposit the same to the credit of Government within the specified date.

4.4 The proposed amendment provides that if any payment on which tax is required to be deducted but not deducted or tax has been deducted but not paid within the due date of filing of Income Tax Return, then, such amount on which tax was liable to be deducted shall not be considered as Application during the financial year.

4.5 30% of the amount shall not be treated as application however any such disallowance would result in increase in taxable income. Because unlike business entities for NGOs any disallowance does not result in taxable income. Therefore, even after disallowance the NGOs income will not become taxable unless the total unspent income including such disallowance exceeds 15% of total income. It may be noted that trusts and NGOs are required to apply 85% of the total income during the year. However if the total unspent income and disallowance put together exceed 15% then such excess amount shall be subjected to tax.

5. NO DISALLOWANCE IF ASSESSEE IS NOT IN DEFAULT

5.1 The amount disallowed due to non-deduction of TDS or non payment of TDS can be considered as an Application in the year in which corresponding tax is deducted and paid or if the NGO can establish that they are not assessee in default under the first proviso to sub-section (1) of section 201 as the person to whom payment has been made:

– has furnished his return of income under section 139

– has taken into account such sum for computing income in such return of income

– has paid the tax due on the income declared by him in such return of income and the person furnishes a certificate to this effect from an accountant in such form as may be prescribed.

5.2 Hence, though the NGO can rectify the default of non-deduction of TDS or non-payment of TDS as per Section 40(a)(ia) and reclaim the amount as application in the year of correction of default but any default of Section 40A(3) & 40A(3A) shall be permanent in nature and shall not be considered as Application in any subsequent year.

6. SECTION 14 AND FIVE HEADS OF INCOME DO NOT APPLY TO NGOS

6.1 The law makers should have understood that Section 14 and five heads of income do not apply to NGOs. It is a settled law that the computation of income of NGOs should be made only under section 11 to 13 the other provisions of the Act are not applicable. It may be noted that under the current scheme of the Income Tax Act, Trust and NGOs are not assessed under five head of income and section 14 which provides for computation under five heads of income does not apply to them. In CIT v. Estate of V. L. Ethiraj [1982] 136 ITR 12 (Mad.), it was held that income from properties would have to be arrived at in the normal commercial manner without reference to the provisions which were attracted by section 14. In this case the Court observed that the language of section 11(1)(a) makes it clear that the income derived from the property held under trust wholly for charitable and religious purposes, to the extent to which such income is applied to such purposes in India, is excluded. When once the income from the property, as such, is excluded, there is no question of computing the income from the property by applying the provisions of section 14.

7. CONCLUDING REMARK

7.1 Linking a section from the chapter pertaining to business and profession will result in needless confusion and controversies. Further, in case of NGOs, unlike other assesses, the taxable income is not computed. The exempt income is only computed therefore any increase of decrease in expenditure does not result in a change in taxable income. This amendment will create lot of assessment controversies as AOs have a tendency to tax the additions, which will not be sustainable in case of NGOs. CBDT will have to come up with adequate clarificatory circulars to capacitate both the AOs and Assesses with regard to the application of these amendments.

RULE 6DD

No disallowance under sub-section (3) of section 40A shall be made and no payment shall be deemed to be the profits and gains of business or profession under sub-section (3A) of section 40A where a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, exceeds ten thousand rupees in the cases and circumstances specified hereunder, namely :—

a) where the payment is made to—

   i. the Reserve Bank of India or any banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);

   ii. the State Bank of India or any subsidiary bank as defined in section 2 of the State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959);

   iii. any co-operative bank or land mortgage bank;

   iv. any primary agricultural credit society or any primary credit society as defined under section 56 of the Banking Regulation Act, 1949 (10 of 1949);

   v. the Life Insurance Corporation of India established under section 3 of the Life Insurance Corporation Act, 1956 (31 of 1956);

b) where the payment is made to the Government and, under the rules framed by it, such payment is required to be made in legal tender;

c) where the payment is made by—

   i. any letter of credit arrangements through a bank;

   ii. a mail or telegraphic transfer through a bank;

   iii. a book adjustment from any account in a bank to any other account in that or any other bank;

   iv. a bill of exchange made payable only to a bank;

   v. the use of electronic clearing system through a bank account;

   vi. a credit card;

   vii. a debit card.

   Explanation.—For the purposes of this clause and clause (g), the term "bank" means any bank, banking company or society referred to in sub-clauses (i) to (iv) of clause (a) and includes any bank [not being a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949)], whether incorporated or not, which is established outside India;

d) where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the asses-see to such payee;

e) where the payment is made for the purchase of—

   i. agricultural or forest produce; or

ii. the produce of animal husbandry (including livestock, meat, hides and skins) or dairy or poultry farming; or

iii. fish or fish products; or

iv. the products of horticulture or apiculture, to the cultivator, grower or producer of such articles, produce or products;

f) where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products;

g) where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, profession or vocation, in any such village or town;

h) where any payment is made to an employee of the assessee or the heir of any such employee, on or in connection with the retirement, retrenchment, resignation, discharge or death of such employee, on account of gratuity, retrenchment compensation or similar terminal benefit and the aggregate of such sums payable to the employee or his heir does not exceed fifty thousand rupees;

i) where the payment is made by an assessee by way of salary to his employee after deducting the income-tax from salary in accordance with the provisions of section 192 of the Act, and when such employee—

i. is temporarily posted for a continuous period of fifteen days or more in a place other than his normal place of duty or on a ship; and

ii. does not maintain any account in any bank at such place or ship;

j) where the payment was required to be made on a day on which the banks were closed either on account of holiday or strike;

k) where the payment is made by any person to his agent who is required to make payment in cash for goods or services on behalf of such person;

l) where the payment is made by an authorised dealer or a money changer against purchase of foreign currency or travellers cheques in the normal course of his business.

Explanation —For the purposes of this clause, the expressions “authorised dealer” or “money changer” means a person authorised as an authorised dealer or a money changer to deal in foreign currency or foreign exchange under any law for the time being in force.]

LANDMARK RULING BY SUPREME COURT REGARDING SET OFF OF PAST DEFICIT

1. INTRODUCTION

1.1 It is now lawfully settled that charitable or religious organisation have the right to claim set off of previous year deficit and losses under Income Tax Act. The current year deficits are also liable to be set off against future year income. For example, if the income of an NPO in the current year is Rs. 1 crore and it has spent Rs. 1.5 crore during the year, then it can offset the deficit of Rs. 0.5 crore against future income by carrying forward the deficit.

1.2 The Supreme Court recently held carry forward deficit of earlier year was admissible for set off against income of subsequent years for charitable and religious organisation. There are various high court citations which have held that a Trust can be allowed to carry forward deficit of current year and to set off same against income of subsequent years.

1.3 Such deficit and losses can be set off against future profits, indefinitely.

2. SUPREME COURT RULING REGARDING SET OFF OF PAST DEFICIT

2.1 The Supreme Court of India in the case Commissioner of Income Tax (Exemption) Vs. Subros Educational Society IT Appeal No. 382 of 2015. (2018) 2 NYPCTR 490 (SC) judgement dated 16th April, 2018 held that any excess expenditure incurred by the trust/charitable institution in earlier assessment year could be allowed to be set off against income of subsequent years for invoking s. 11.

2.2 The Apex Court examined the following questions "(a) Whether any excess expenditure incurred by the trust/charitable institution in earlier assessment year could be allowed to be set off against income of subsequent years by invoking s. 11 of the IT Act, 1961 ?"

2.3 The court did not find any merit in the contention of revenue and held that past deficit were legitimate applications eligible for set off against current year income. This decision settles the continuing controversy regarding set off of past deficit.

3. VARIOUS COURT CASES IN FAVOUR OF NPOS

3.1 In the case of DIT v. Raghuvanshi Charitable Trust [2011] 197 TAXMAN 170 (Delhi) the High Court of Delhi also held that a Trust can be allowed to carry forward deficit of current year and to set off same against income of subsequent years. It was further held that adjustment of deficit of current year against income of subsequent year would amount to application of income of Trust for charitable purposes in subsequent year within meaning of section 11(1)(a). The cases Siddaramanna Charities Trust v. CIT [1974] 96 ITR 275 (Mys.) and CIT v. Matriseva Trust [2000] 242 ITR 20 /[2003] 128 Taxman 261 (Mad.) are also relevant. Further, it has been held that excess of expenditure over income of charitable or religious nature incurred in earlier years can be adjusted against the income of the current year. This issue was debated in CIT v. Maharana of Mewar Charitable Foundation [1987] 164 ITR 439 (Raj.), and it was opined that application could be considered to have taken place in the year of adjustment, where the earlier year's income was not adequate to absorb the actual expenditure made. Thus, a distinction between actual expenditure and application, for the purposes of section 11(1)(a) was made.

3.2 The Court in the case CIT v. Maharana of Mewar (supra) referred to a CBDT Circular, dated 24-1-1973 wherein it was clarified that the repayment of loans taken for meeting certain expenditures of earlier years could be considered as application. The Court was of the opinion that in the light of the aforesaid circular, if set off of past years' deficit was not allowed then it would lead to an anomalous situation, where if the Trust took a loan for the purposes of incurring expenses for charitable and religious purposes in a particular year and the said loan was repaid out of the income of the subsequent year, the said repayment would be entitled to exemption from tax under section 11(1)(a) of the Act. On the contrary, if the Trust, instead of taking a loan, incurred expenditure for charitable and religious purposes out of the corpus of the Trust and sought to reimburse the said amount out of the income of the subsequent year, the Trust would not be entitled to claim exemption in respect of such reimbursement under section 11(1)(a) of the Act.

3.3 Therefore, the Court held that it would be incorrect to view the term 'application' from a narrow perspective so as to relate it with the actual movement of funds. The relevant extracts of the case are as follows:

". . . there is nothing in the language of section 11(1)(a) which lends support to the contention. . . that the expenditure incurred in the earlier year cannot be met out of the income of the subsequent year and utilisation of such income for meeting the expenditure of the earlier year would not amount to such income being applied for charitable or religious purposes. . . the words used in section 11(1)(a) must be given their natural meaning. The word 'applied' as defined in Chambers' Dictionary means 'to put to use' or 'to turn to use'. According to the Oxford Dictionary, the word 'applied' means 'to make use' or 'to put to practical use'. When the income of a Trust is used or put to use to meet the expenses incurred for religious or charitable purposes, it is applied for charitable or religious purposes. The said application of the income for charitable or religious purposes takes place in the year in which the income is adjusted to meet the expenses incurred for charitable or religious purposes. In other words, even if the expenses for charitable and religious purposes have been incurred in the earlier year and the said expenses are adjusted against the income of a subsequent year, the income of that year can be said to have been applied for charitable and religious purposes in the year in which the expenses incurred for charitable and religious purposes had been adjusted.

. . . the adjustment of the expenses incurred by the Trust for charitable and religious purposes in the earlier year against the income earned by the Trust in the subsequent year would amount to applying the income of the Trust for charitable and religious purposes in the subsequent year in which such adjustment has been made and will have to be excluded from the income of the Trust under section 11(1)(a) of the Act." (p. 442)

3.4 In CIT v. Shri Plot Swetamber Murti Pujak Jain Mandal [1994] 119 CTR (Guj.) 144, Circular No. 100, dated 24-1-1973 which allowed repayment of loan taken in earlier years for fulfilment of charitable objects as application was referred to. The Court held that the same principle should apply if instead of taking loan the organisation spend money out of its corpus and it is reimbursed in subsequent years There is nothing in section 11(1)(a), which shall indicate that the expenditure incurred in the earlier year cannot be met out of the income of subsequent years. Some relevant extracts of the case are as under:

"According to the above referred circular if a Trust wants to spend more money for charitable and religious purposes in a particular year, it can take a loan and the said loan can be repaid out of the income of the subsequent year and the payment of the said loan out of the income of the subsequent year would amount to application of income for charitable and religious purposes under section 11(1)(a) of the Act. The contention that only that part of the income of a charitable Trust should be excluded which was applied for charitable and religious purposes during the relevant assessment year in which the income was earned, cannot be accepted, as it would lead to an anomalous situation. If the Trust takes a loan for the purposes of incurring expenses for charitable and religious purposes in a particular year and the said loan is repaid out of the income of the subsequent year, the said repayment would be entitled to exemption from tax under section 11(1)(a) of the Act in view of the above referred to circular. But, if the Trust instead of taking a loan incurs expenses for charitable and religious purposes out of the corpus of the Trust and seeks to reimburse the said amount out of the income of the subsequent year, the Trust would not be entitled to claim exemption in respect of such reimbursement under section 11(1)(a) of the Act if the contention advanced by the Revenue is accepted. The construction which leads to such an anomaly has got to be avoided. There is nothing in the language of section 11(1)(a) of the Act to indicate that the expenditure incurred in the earlier year cannot be met out of the income of the subsequent year or that utilization of such income for meeting the expenditure of the earlier year, would not amount to such income being applied for charitable or religious purposes." (p. 148)

3.5 There is no judicial or statutory bar on setting off the deficit of earlier years against the income of current year if the return of income has been filed within the prescribed time. This has also been confirmed by the Bombay High Court in CIT v. Institute of Banking Personnel Selection (IBPS) [2003] 264 ITR 110/131 Taxman 386, wherein it was held that income derived from a Trust property should be computed on sound commercial principles and this included carrying-forward and set-off of deficit in the earlier years. The relevant extract is as under :

"Income derived from the Trust property has also got to be computed on commercial principles and if commercial principles are applied, then adjustment of expenses incurred by the Trust for charitable and religious purposes in the earlier years against the income earned by the Trust in the subsequent year will have to be regarded as application of income of the Trust for charitable and religious purposes in the subsequent year in which adjustment has been made having regard to the benevolent provisions contained in section 11 and such adjustment will have to be excluded from the income of the Trust under section 11(1)(a). Accordingly, on the facts and in the circumstances of the instant case, the Tribunal was justified in law in allowing carrying forward of the deficit of earlier year and set it off against the surplus of subsequent years."

3.6 The Madhya Pradesh High Court in the case Commissioner of Income-tax v. Gujrati Samaj (Regd.) 349 ITR 559 (MP) [2012], 31 taxmann.com 68 (MP) [2013] it was held that expenses for charitable purposes incurred in earlier year are eligible to be adjusted against income of a subsequent year, income of that year can be said to have been applied for charitable purposes in the year in which expenses has been adjusted. The relevant extract is provided as under :

"In view of section 11(1)(a), it cannot be said that the expenditure incurred in the earlier year cannot be met out of the income of the subsequent year and utilization of such income for meeting the expenditure of the earlier year would not amount to such income being applied for charitable or religious purposes. Having regard to section 11(1)(a) of the Act, when the income of the Trust is used or put to use to meet the charitable or religious purposes, it is applied for charitable purpose and the said application of the income for charitable or religious purposes takes place in the year in which the income is adjusted to meet the expenses incurred for charitable or religious purposes. Thus, even if the expenses for charitable and religious purposes have been incurred in the earlier year and the said expenses are adjusted against the income of the subsequent year, the income of that year can be said to have been applied for charitable and religious purposes in the year in which expenses incurred for charitable and religious purposes had been adjusted. There are no words of limitation in section 11(1)(a) of the Act explaining that the income should have been applied for charitable or religious purposes only in the year in which the income had arisen. [Para 8]"

3.7 In the case of Delhi Tribunal in the case of Pushpawati Singhania Research Institute for "Liver, Renal & Digestive Diseases v. DDIT (Exemption) [2009] 29 SOT 316 (Del) it was held that when income accumulated in an earlier year cannot qualify for exemption under section 11(2) the excess income applied in earlier assessment year will also not qualify for exemption. The ruling of Delhi Tribunal is not relevant as far as the normal set off of deficit is concerned, because the Delhi Tribunal case is in a different context, in this case it was held that when income accumulated in an earlier year cannot qualify for exemption under section 11(2) then deficit of earlier assessment year will also not qualify for exemption. In other words, the Tribunal denied set off expenditure pertaining to that portion of income which was subjected to tax under section 11(2), therefore, this case does not affect the deficit carried forward in normal cases.

4. CONTRARY RULING WHICH STANDS NULLIFIED

4.1 In the case Anjuman-E-Himayath-E-Islam v. Assistant Director of Income-tax (Exemption)-IV, Chennai [2015] 59 taxmann.com 379 (Chennai - Trib.) it was held that excess application of funds over and above income of trust can arise only when funds are applied from the corpus of the trust, accumulated funds, loans or goods and services received from the creditors. When funds are applied from borrowed funds or by way of sundry creditors the same can be treated as application of funds in the year in which such loan/sundry creditors are repaid from the income of the trust. However, when amount is applied from the corpus fund or accumulated fund the same cannot be treated as application of funds under section 11, because such funds have already been exempt from the income of trust in the year in which they are received or such amount is set aside. Thus, trust cannot carry forward excess application of funds. This Chennai Tribunal decision was controversial in nature and has now been nullified by the Supreme Court ruling (supra).

REVIEW PETITION UNDER FCRA AGAINST NON-RENEWAL OR CANCELLATION

1. INTRODUCTION

1.1 Whenever the FCRA (Foreign Contribution Regulation Act, 2010) registration is cancelled or not renewed the affected organisation either has to silently accept the decision or in rare circumstances approach the High Court. It has been seen that both non renewal and cancellation orders have been passed in the past without providing speaking reasons.

1.2 It may be noted that under the FCRA 2010 the FCRA Division of MHA (Ministry of Home Affairs) is duty bound to provide specific reasons for non-renewal and cancellation. The FCRA 2010 does not permit arbitrary or discretionary non-renewal or cancellation.

1.3 The provisions of renewal FCRA registration are provided in Section 16 of FCRA 2010, which clearly provides that renewal may not be granted if there is any violation of FCRA 2010 and FCRA Division of MHA has to provide the reason in case there is non-renewal. In other words, it is necessary to establish that there was violation of FCRA 2010 for passing any coercive order, which results in non-renewal of FCRA 2010.

1.4 Similarly, under section 14 (explained hereunder) provides five specific circumstances under which an FCRA Certificate can be cancelled after appropriate inquiry and due opportunity of being heard.

1.5 In the light of the above if an organisation finds that non-renewal or cancellation of FCRA registration was made without following the provisions of FCRA 2010, then it is advisable to file a review petition under section 32 of the FCRA, 2010. A review petition is an lawful remedy available under the act and the senior authorities at the FCRA Department may reverse the order if they are convinced that the law was not properly followed regarding non-renewal or cancellation of FCRA registration.

2. REVIEW PETITION AGAINST CANCELLATION OR NON RENEWAL

2.1 Under FCRA, 2010 an organisation whose registration has been cancelled under section 14 or not renewed under section 17 can, apart from the appellate remedy, also apply for a review of the cancellation order. It is advisable to file a formal review petition U/s. 32(1) of the FCRA, 2010 for restoration of the registration. A review petition under section 32 of FCRA is made in plain paper as per Rule 20 with a fee of Rs. 1000/- payable in favour of 'Pay and Accounts Officer, Ministry of Home Affairs", payable at New Delhi. Such petition should be accompanied by the evidence of FC return filed for the last 5 years.

2.2 Legally the aggrieved organisations can also appeal to the High Court. However, it has been seen in the past that the FCRA department has restored the registration of many compliant organisations on filing of a review petition. The text of section 32 is provided as under:

Revision of orders by Central Government.

32(1)The Central Government, may, either of its own motion or on an application for revision by the person registered under this Act, call for and examine the record of any proceeding under this Act in which any such order has been passed by it and may make such inquiry or cause such inquiry to be made and, subject to the provisions of this Act, may pass such order thereon as it thinks fit.

(2) The Central Government shall not of its own motion revise any order under this section if the order has been made more than one year previously.

(3) In the case of an application for revision under this section by the person referred to in sub-section (1), the application must be made within one year from the date on which the order in question was communicated to him or the date on which he otherwise came to know of it, whichever is earlier:

Provided that the Central Government may, if it is satisfied that such person was prevented by sufficient cause from making the application within that period, admit an application made after the expiry of that period.

(4) The Central Government shall not revise any order where an appeal against the order lies but has not been made and the time within which such appeal may be made has not expired or such person has not waived his right of appeal or an appeal has been filed under this Act.

(5) Every application by such person for revision under this section shall be accompanied by such fee, as may be prescribed.

Explanation—An order by the Central Government declining to interfere shall, for the purposes of this section, be deemed not to be an order prejudicial to such person.

A review petition has to be made within a period of one year. Further an appeal and review petition cannot be made simultaneously, the organisation has to waive its right to appeal before making a review petition. Further, though there is no specific provision regarding appeal against rejection of review petition, in our opinion the organisation shall be entitled to file a writ petition before the High Court in deserving cases.

3. HOW TO PREPARE A REVIEW PETITION

3.1 A review petition should be drafted as per the provisions of section 32 of the FCRA, 2010. A sample format of the review petition is provided in the Annexure 1.

3.2 The application must be made within one year from the date on which the order in question was communicated to him or the date, on which he otherwise came to know of it, whichever is earlier.

3.3 Kindly make a payment of Rs. 1,000/- in favour of "Pay & Accounts Officer, Ministry of Home Affairs" payable at Delhi, as per Rule 20 of FCR Rules 2016.

4. CANCELLATION OF REGISTRATION CERTIFICATE

4.1 Under section 14, of FCRA 2010 the Central Government may cancel the registration certificate for various reasons. However, no certificate shall be cancelled unless reasonable opportunity of being heard is provided. The provision of section 14 on cancellation of registration certificate is as under :

"14.(1) The Central Government may, if it is satisfied after making such inquiry as it may deem fit, by an order, cancel the certificate if —

– the holder of the certificate has made a statement in, or in relation to, the application for the grant of registration or renewal thereof, which is incorrect or false; or

– the holder of the certificate has violated any of the terms and conditions of the certificate or renewal thereof; or in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate; or

– the holder of certificate has violated any of the provisions of this Act or rules or order made thereunder; or

– in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate; or

– if the holder of the certificate has not been engaged in any reasonable activity in its chosen field for the benefit of the society for two consecutive years or has become defunct.

2. No order of cancellation of certificate under this section shall be made unless the person concerned has been given a reasonable opportunity of being heard.

3. Any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate."

4.2 The Central Government may, if it is satisfied after making such inquiry as it may deem fit, by an order, cancel the certificate if the reason(s) as specified above are found to be correct.

4.3 Section 14(1)(d) above does not prescribe that the organisation should have been engaged in its activities by spending FC funds. Therefore, even if the organisation had not been engaged in any reasonable activity for two consecutive years in spending its FC funds, if any, but had been reasonably active carrying out its activities through domestic funds, then the organisation may be allowed to continue with the registration certificate if adequate reasons for such continuation are provided.

5. OPPORTUNITY OF BEING HEARD

5.1 No order of cancellation of certificate under this section shall be made unless the person concerned has been given a reasonable opportunity of being heard.

6. RE-APPLICATION FOR REGISTRATION AFTER CANCELLATION

6.1 Any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate. Any such application will be accepted only after 3 years.

Annexure-1

SAMPLE FORMAT OF A REVIEW PETITION UNDER SECTION 32

REVISION PETITION U/S 32 OF FCRA 2010 FOR REVIEW OF ORDER OF REJECTION OF RENEWAL OF REGISTRATION

The Secretary,
Ministry of Home Affairs (FCRA Wing)
1st Floor, Major Dhyan Chand National Stadium,
Near Pragati Maidan, New Delhi-110001

Re: Petition for Review u/s 32 of Foreign Contribution Regulation Act, 2010 of Non- Renewal of Application for Renewal of Registration. Name of Association: XYZ.........................., FC Registration No.000000000 Dt...................

Ref: MHA File No. ....
Sub.: Denial of Application for Renewal.

Dear Sir,
Facts & History:

1.1. XYZ......................... is a charitable organization duly registered under FCRA since .... Copy of FCRA Registration Certificate provided in Annexure 1.

1.2. XYZ......................... is also registered under section 12AA of the Income Tax Act bearing Registration No……………………… It continues to remain the compliant tax exempt charity under Income Tax Law. Copy of 12AA Registration Certificate provided in Annexure 2.

1.3 XYZ......................... has been filing audited statements and annual returns as per the law. There are no proceedings pending against it under the FCRA Law. The copy of the annual return form and financial statement for past 5 years is provided in Annexure 3.

1.4. XYZ......................... applied for Renewal of Registration on ...., the acknowledgement receipt from MHA website is provided in Annexure 4.

1.5. The application for Renewal of Registration was not renewed on ...., the reasons provided was as under:

“Your application No............................... has been refused due to following reasons: On the basis of Field agency report, the competent authority has decided to refuse your application for renewal.”

The snapshot of the email communication is provided in Annexure 5.

We humbly submit the petition for review u/s 32 of Foreign Contribution Regulation Act, 2010 of Non-Renewal of Application for Renewal of Registration.

Overview of the Activities:

....

.... A detailed overview of activities is provided in Annexure 11.

Declaration regarding the lawfulness of activities

3.1. We hereby declare that all our activities are completely in compliance with the Foreign Contribution Regulation Act, 2010 and are totally in interest of India.

3.2. We have not engaged in any activity which violates FCRA, 2010.

3.3. We have not worked with any organization directly or indirectly whose activity have been held or perceived to be held against the National Interest of India.

Issues & Questions of Law

4.1. That XYZ......................... is not aware of any violation or inquiry under FCRA being initiated against it. No show cause has ever been provided to XYZ......................... for any possible violation of FCRA Laws.

4.2. It is humbly submitted that the second proviso to section 16 of the FCRA Act, 2010 clearly provides that Renewal of Registration can be refused only if a person has violated any of the provisions of the FCRA 2010. The second proviso to section 16 of the FCRA Act, 2010 is reproduced as under:

"Provided further that the Central Government may refuse to renew the certificate in case where a person has violated any of the provisions of this Act or rules made thereunder."

In the light of the above provision the renewal application can only be denied if there is any violation of any of the provisions of this Act or rules made thereunder.

4.3. It is further humbly submitted and reiterated that no notice or any adverse report or finding against XYZ......................... was ever served upon us and therefore it cannot be treated that there is violation of any provisions of the FCRA Laws.

4.4. No opportunity being heard was provided to XYZ......................... against such non-renewal FC registration which has rendered irreparable financial hardship to the organisation and its activity. As a result the staffs and beneficiaries of XYZ......................... are suffering.

4.5. The action of non-renewal has been taken without proper application of the applicable provisions of FCRA, 2010.

4.6. The petitioner humbly submits that an opportunity of being heard was not provided before the coercive measure of non renewal was taken.

Prayer

It is humbly prayed that the non-renewal of the application for renewal may be reviewed and revised and the petitioner may be granted regular registration.

Thanking You,
Yours sincerely,
For XYZ..........................

FCRA NOTIFICATION ON PROSECUTION & COMPOUNDING OF OFFENCE

1. INTRODUCTION

1.1 Ministry of Home Affairs has issued a Notification No. S.O. 2291(E), dated 05.06.2018 regarding the various authority for compounding of offences before initiating any prosecution. The text of the circular is provided in Annexure 1.

1.2 It may be noted that earlier, though, the Foreign Contribution Regulation Act, 2010 (FCRA 2010) provided for compounding of offence but there was no clarity about the administrative hierarchy in dealing such issues. Now with the issue of this notification there is

– a section wise and offence wise clarity regarding the various offences

– clarity about the type of offence and the quantum of penalty

– clarity about the specific authority who has the power to dispose such cases.

2. HIGHLIGHTS OF THE NOTIFICATION

2.1 The aforesaid notification supercedes all earlier notifications and circulars pertaining to compounding of offences. This notification has provided for compounding of various new offences which were not notified earlier. In some sense it is a positive move and provides clarity about the possible penalty in case of a violation. The offences, quantum and the authority in nutshell is as under:

– Accepting foreign hospitality without approval shall be subject to a penalty of Rs. 10,000/- and such cases can be disposed of by the Director or Deputy Secretary in charge.

– Transferring foreign fund to unauthorised recipients shall be subject to a penalty of Rs. 1,00,000/- or 10% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.

– If the administrative expenses exceeds 50% of contribution received then the excess amount shall be subject to a penalty of Rs. 1,00,000/- or 5% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.

– If foreign contribution is received without registration or prior permission then it shall be subject to a penalty of Rs. 1,00,000/- or 10% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.

– If the foreign contribution in received in any account other than the designated bank account then such amount shall be subject to a penalty of Rs. 1,00,000/- or 5% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.

– If the bank or authorised person fail to inform regarding any unauthorised receipt of foreign contribution then bank or authorised person shall be subject to a penalty of Rs. 1,00,000/- or 3% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.

- If local fund is deposited in the FC account then it shall be subject to a penalty of Rs. 1,00,000/- or 2% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.
- If an organisation or person fails to provide intimation to FCRA Department regarding the source of foreign contribution received then it shall be subject to a penalty of Rs. 1,00,000/- or 5% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.
- If an organisation or person fails to maintain books of accounts and records regarding foreign contribution received then it shall be subject to a penalty of Rs. 1,00,000/- or 5% whichever is higher and such cases can be disposed of by the Director or Deputy Secretary in charge.

3. SUMMARISED OVERVIEW OF THE LAW PERTAINING TO COMPOUNDING OF OFFENCE

3.1 The Foreign Contribution Regulation Act, 2010 (FCRA) provides for compounding of offences. This new provision would provide relief to many organisations who commit violation, sometimes, unintentionally. Under the new provisions, organisations who have violated the provisions of FCRA can resolve their case by paying financial penalties only. Some highlight of the new provisions are as under

- Under the old FCRA law organisations were being prosecuted, even, for small offences such as receiving FC funds in the non FC bank account. There are instances where organisations have fought cases for decades together against petty offences.
- The new FCRA provides that most of the offences (except those, which are subject to imprisonment only) can be resolved by payment of financial penalty.
- any such offence may, before the institution of any prosecution, be compounded against payment of specified sums.
- Once an offence is compounded, the same person cannot avail the benefit of compounding if such offence is committed again within three years.
- However, if an offence is committed after three years of compounding, then such subsequent offence will be treated as first offence and can be compounded again.
- The Director or Deputy Secretary in charge of FCRA Wing, Ministry of Home affairs shall be the authority for exercising the powers of compounding of an offence.
- The option to compound and close an offence without prosecution is a welcome change. This provision shall provide relief to both the Government Authorities and the litigants, as offences could be resolved lawfully without fighting, time consuming legal cases.

4. STATUTORY PROVISION ON COMPOUNDING OF OFFENCES

4.1 Section 41 of the FCRA 2010 provides that any offence punishable under this Act (whether committed by an individual or organisation, not being an offence punishable with imprisonment only, may, before the institution of any prosecution, be compounded by such officers or authorities and for such sums as the Central Government may, by notification in the official gazette, specify.

4.2 The text of Section 41 is reproduced as under:

"Section 41 : Compounding of certain offences:

(1) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence punishable under this Act (whether committed by an individual or association or any officer or employee thereof), not being an offence punishable with imprisonment only, may, before the institution of any prosecution, be compounded by such officers or authorities and for such sums as the Central Government may, by notification in the official gazette, specify in this behalf.

(2) Nothing in sub-section (1) shall apply to an offence committed by an individual or association or its officer or other employee within a period of three years from the date on which a similar offence committed by it or him was compounded under this section.

Explanation–For the purposes of this section, any second or subsequent offence committed after the expiry of a period of three years from the date on which the offence was previously compounded, shall be deemed a first offence.

(3) Every officer or authority referred to in sub-section (1) shall exercise the powers to compound an offence, subject to the direction, control and supervisions of the Central Government.

(4) Every application for the compounding of an offence shall be made to the officer or authority referred to in sub-section (1) in such form and manner along with such fee as may be prescribed.

(5) Where any offence is compounded before the institution of any prosecution, no prosecution shall be instituted in relation to such offence, against the offender in relation to whom the offence is so compounded.

(6) Every officer or authority referred to in sub-section (1), while dealing with a proposal for the compounding of an offence for a default in compliance with any provision of this Act which requires by an individual or association or its officer or other employee to obtain permission to file or register with or deliver or sent to, the Central Government or any prescribed authority any return account or other document, may, direct by order, if he or it thinks fit to do so, any individual or association or its officer or other employee to file or register with, such return, account or other document within such time as may be specified in the order."

5. OFFENCES THAT CAN BE COMPOUNDED AND PENALTIES THEREOF

5.1 In terms of Gazette Notification No. S.O. 2291(E), dated 05.06.2018 , the categories of offences that can be compounded under section 41 of FCRA, 2010 and the quantum of penalty for compounding, as indicated against each of the offences, is provided in Annexure 1.

5.2 Apart from the above-specified penalties, the Director or Deputy Secretary in charge of FCRA Wing, Ministry of Home affairs shall be the authority for exercising the powers of compounding of an offence. In other words, apart from the offences mentioned in Annexure 1 the Director or Deputy Secretary of FCRA department has the authority to compound all other offences, except those offences which are subject to imprisonment only.

6. HOW TO APPLY FOR COMPOUNDING OF AN OFFENCE UNDER FCRA 2010

6.1 An application for the compounding of an offence under section 41 is to be made to the Secretary, Ministry of Home Affairs, New Delhi on a plain paper along with a fee of '1000/- (One Thousand only) in the form of a demand draft or a banker's cheque in favour of the "Pay and Accounts Officer, Ministry of Home Affairs", payable at New Delhi. It may be noted that, formally FCRA department has become a paper less department but no mechanism has been provided for an application for the compounding of an offence under section 41. The affected organisation is advised to contact FCRA department over mail before sending the hard copies.

6.2 It may be noted that currently FCRA is a paperless department; however, no online procedure has been provided for Compounding of Offences. Therefore, an organisation should right to the FCRA department before filing any such petition.

7. WHAT HAPPENS AFTER AN OFFENCE IS COMPOUNDED

7.1 After payment of the penalty imposed and compounding of the offence, the person may be granted registration or prior permission, as the case may be, subject to its fulfilling all parameters.

8. WHAT IF THE PERSON IS UNWILLING OR UNABLE TO PAY THE PENALTY IMPOSED

8.1 In the event of failure to pay the penalty, for whatever reason, necessary action for prosecution of the person shall be initiated.

Annexure-1

GAZETTE NOTIFICATION NO. S.O. 2291(E), DATED 5.06.2018

MINISTRY OF HOME AFFAIRS
NOTIFICATIONS
New Delhi, the 5th June, 2018

S.O. 2291(E), – In exercise of the powers conferred by sub-section (1) of Section 41 of the Foreign Contribution (Regulation) Act, 2010 (42 of 2010) and in supersession of the notifications of the Government of India in the Ministry of Home Affairs numbers S.O. 1976(E), dated the 26th August, 2011 and S.O. 2133(e), dated the 16th June, 2016, published in the Gazette of India, Extraordinary, Part-II, Section 3, Sub-section (ii), except as respects things done or omitted to be done before such supersession, the Central Government hereby specifies the officer in column (4) of the table, who may, before institution of any prosecution under the Act, compound the offences specified in column (4) of the table, who may, before institution of any prosecution under the Act, compound the offences specified in column (2), on payment of the amount specified in column (3), of the said table namely:-

TABLE

Sr. No.	Offence	Amount of Penalty	Officer competent for compounding
(1)	(2)	(3)	(4)
1.	Offence punishable under section 35 for accepting any hospitality in contravention of section 6 of the Act	Rs. 10,000/-	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
2.	Offence punishable under section 37 for transferring any foreign contribution to any other person in contravention of section 7 of the Act or any rule made thereunder.	Rs. 1,00,000/- or 10% of such transferred foreign contribution, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
3.	Offence punishable under section 37 for defraying of foreign contribution beyond fifty per cent of the contribution received for administrative expenses in contravention of section 7 of the Act.	Rs. 1,00,000/- or 5% of such foreign contribution so defrayed beyond the permissible limit, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
4.	Offence punishable under section 35 for accepting foreign contribution is contravention of section 11 of the Act.	Rs. 1,00,000/- or 10% of the foreign contribution received, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
5.	Offences punishable under section 37 read with section 17 of the Act for (a) receiving foreign contribution in any account other than specified account in his application for grant of certificate.	Rs. 1,00,000/- or 5% of the foreign contribution received in such account, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.

Sr. No.	Offence	Amount of Penalty	Officer competent for compounding
(1)	(2)	(3)	(4)
(b)	non-reporting the prescribed amount of foreign remittance of secure and manner of such remittance by banks and authorised persons.	Rs 1,00,000/- or 3% of the foreign contribution received or deposited in such account, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
(c)	receiving & depositing any fund other than foreign contribution in the account or accounts opened for receiving foreign contribution or for utilizing the foreign contribution.	Rs. 1,00,000/- or 2% of such deposit, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
6.	Offence punishable under section 37 for non-furnishing of intimation of the amount of each foreign contribution received and the source from which and in the manner in which, such foreign contribution is received as required under section 18 of the Act.	Rs. 1,00,000/- or 5% of the foreign contribution received during the period of non-submission, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.
7.	Offence punishable under section 37 for not maintaining the account and records of foreign contribution received and manner of its utilisation on required section 19 of the Act.	Rs. 1,00,000/- or 5% of the foreign contribution during the relevant period of the non-maintainance of accounts, whichever is higher.	Director, or as the case may be, the Deputy Secretary in-charge of the section responsible for the administration of the Act.

2. In case more than one offence has been committed by a person, the total amount of the compounding for such offences shall not be more than the value of the foreign contribution involved.

[F.No. II/21022/23(088)/2015-FCRA-III(A)]
SANTOSH SHARMA, Director (FCRA)

CONSOLIDATION OF ACCOUNTS IN A SECTION 8 HOLDING COMPANY

1. INTRODUCTION

1.1 Under section 129(3) of the Companies Act, 2013 it is mandatory to prepare consolidated financial statements in addition to Standalone Financial Statements b('SFS'), in case where the company has one or more subsidiaries. In other words, the holding company is required to incorporate the financial statements of all its subsidiaries and prepare consolidated financial statements.

1.2 A Section 8 company (a company registered as a not for profit charity) can also have subsidiary companies. It is not clear whether the section 8 holding company is also required to prepare consolidated financial statements. The common understanding is that the same procedure will also apply to the section 8 company. However, on careful analysis of the statute and the applicable Accounting Standards it seems that where one section 8 company is the holding company of another section 8 company, the requirement of consolidation of financial statements shall not apply, which is discussed in this issue.

2. THE ASSETS OR INCOME CANNOT REVERT TO THE MEMBERS OF SECTION 8 COMPANIES

2.1 Section 8 companies are formed with charitable objects and the profits of a subsidiary cannot be distributed back to the members including a holding company. Section 8 companies are formed without profit motive. However if there is any profit/ surplus, then such profit/surplus shall be applied in promoting its objects.

2.2 At the time of winding up or dissolution, surplus assets, if any, shall be transferred to another company registered under Section 8 having similar objects.

2.3 In case of conversion of a Section 8 company into any other kind of company (except a One Person Company), the Board of directors are required to give a declaration to the effect that no portion of the income or property of the company has been or shall be paid or transferred directly or indirectly by way of dividend or bonus or otherwise to persons who are or have been members of the company or to any one or more of them or to any persons claiming through any one or more of them [Rule 22(4) of Companies (Incorporation) Rules, 2014].

3. UNDERSTANDING SECTION 129 OF THE COMPANIES ACT, 2013

3.1 A holding company of a Section 8 company is not entitled to any share in profits or income of its subsidiary. One of the primary purpose of consolidation is to reflect the correct picture of the value of investment in the subsidiary company. If the value of shares in subsidiary company is reflected through consolidation of the assets and liabilities, then it will show an incorrect picture of the net worth of the holding company as it cannot claim anything from the subsidiary. Further the investment in a section 8 company should be shown as application of income and technically should not remain as investment in the balance sheet.

3.2 When we consolidate the holding company with a Section 8 company, it will however depict a wrong picture of the wealth of the holding company, as the holding company can never claim any right over the profits of a Section 8 Company. Therefore, the question of consolidation does not arise.

3.3 Section 129 mandates preparation of CFS in accordance with applicable accounting standards as is evident from the sub section (1) of section 129, as reproduced below:

"(1) The financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III:

Provided that the items contained in such financial statements shall be in accordance with the accounting standards."

Therefore the provisions of applicable Accounting Standards have to be read with section 129 of the Companies Act 2013.

4. UNDERSTANDING ACCOUNTING STANDARD 21 ISSUED UNDER COMPANIES RULES

4.1 Accounting Standards issued by Companies (Accounting Standards) Rules, 2006 under the erstwhile Companies Act, 1956 are applicable to companies which are not covered under IND AS. It may be noted that Rule 4 of the Companies (Indian Accounting Standards) Rules 2015 makes IND AS mandatory only for certain large corporates. For all other companies the provisions of AS 21 shall apply. The applicability of AS 21 on consolidation of a Section 8 subsidiary, the following is relevant:

4.2 AS 21 clearly states, "This Standard should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent."

4.3 The requirement of consolidation is dependent on the control of the holding company as per the criteria provided in the standard.

4.4 In the scope of the AS 21 it has been clarified when control does not yield any economic benefit then AS 21 is not intended to apply to such entities. The relevant extract from AS 21 is as under:

"Control exists when the parent owns, directly or indirectly through subsidiary (ies), more than one-half of the voting power of an enterprise. Control also exists when an enterprise controls the composition of the board of directors (in the case of a company) or of the corresponding governing body (in case of an enterprise not being a company) so as to obtain economic benefits from its activities. An enterprise may control the composition of the governing bodies of entities such as gratuity trust, provident fund trust etc. Since the objective of control over such entities is not to obtain economic benefits from their activities, these are not considered for the purpose of preparation of consolidated financial statements."

4.5 This scope of AS 21 as defined by the Institute of Chartered Accountants of India clearly excludes the control over those entities from were economic benefit are not permissible. The same rationale shall apply to charitable trust and companies also.

4.6 Further under para 11 of the AS 21 it is again clarified that the consolidation shall not be necessary if there are permanent restrictions on the subsidiary regarding transfer of profits to the holding company. The exceptions as provided in AS 21 are as under:

11. A subsidiary should be excluded from consolidation when:

– control is intended to be temporary because the subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future; or

– it operates under severe long-term restrictions which significantly impair its ability to transfer funds to the parent.

4.7 In consolidated financial statements, investments in such subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments. The reasons for not consolidating a subsidiary should be disclosed in the consolidated financial statements In the light of the above it is clear that consolidation of accounts shall not be necessary in case of section 8 company. The text of AS 21 is provided in Annexure.

5. APPLICABILITY OF IND AS110

5.1 The Ind AS 110 as may be applicable to companies also specifically defines the term control for the purposes of consolidation of accounts. The term control as per Ind AS 110 is as under:

– An investor, regardless of the nature of its involvement with an entity (the investee), shall determine whether it is a parent by assessing whether it controls the investee.

– An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

– Thus, an investor controls an investee if and only if the investor has all the following:

a. power over the investee (see paragraphs 10–14);

b. exposure, or rights, to variable returns from its involvement with the investee (see paragraphs 15 and 16); and

c. the ability to use its power over the investee to affect the amount of the investor's returns (see paragraphs 17 and 18).

d. As provided above under para 7 all the three conditions should be satisfied in order to establish that the investor controls the investee. The condition 7(b) and 7(c) relate to the exposure to return on investment and the ability to affect the amount of the investor's returns. Both these conditions do not apply to a section 8 company.

6. CONCLUDING REMARKS

6.1 It can be seen that the statutory requirements for consolidation are primarily with the intent of providing a true and fair view of the investment of the holding company in its subsidiaries. However in case of section 8 companies, there is no question of investing and change in value of investment as the promotors and share holders cannot claim the amount invested in the shares of a section 8 company. Any amount contributed to a section 8 company is an irrevocable legal obligation for public charitable purposes.

6.2 Therefore in the light of above analysis, in our opinion it is not necessary to consolidate the financial statements of a section 8 company which is the holding company of another subsidiary section 8 company.

Annexure-1

TEXT OF SECTION 129 COMPANIES ACT 2013
FINANCIAL STATEMENT

129. (1) The financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III:

Provided that the items contained in such financial statements shall be in accordance with the accounting standards:

Provided further that nothing contained in this sub-section shall apply to any insurance or banking company or any company engaged in the generation or supply of electricity, or to any other class of company for which a form of financial statement has been specified in or under the Act governing such class of company:

Provided also that the financial statements shall not be treated as not disclosing a true and fair view of the state of affairs of the company, merely by reason of the fact that they do not disclose—

a. in the case of an insurance company, any matters which are not required to be disclosed by the Insurance Act, 1938 (4 of 1938), or the Insurance Regulatory and Development Authority Act, 1999 (41 of 1999);

b. in the case of a banking company, any matters which are not required to be disclosed by the Banking Regulation Act, 1949 (10 of 1949);

c. in the case of a company engaged in the generation or supply of electricity, any matters which are not required to be disclosed by the Electricity Act, 2003 (36 of 2003);

d. in the case of a company governed by any other law for the time being in force, any matters which are not required to be disclosed by that law.

   1. At every annual general meeting of a company, the Board of Directors of the company shall lay before such meeting financial statements for the financial year.

   2. Where a company has one or more subsidiaries, it shall, in addition to financial statements provided under sub-section (2), prepare a consolidated financial statement of the company and of all the subsidiaries in the same form and manner as that of its own which shall also be laid before the annual general meeting of the company along with the laying of its financial statement under sub-section (2):

Provided that the company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries in such form as may be prescribed 17:

Provided further that the Central Government may provide for the consolidation of accounts of companies in such manner, as may be prescribed18.

Explanation —For the purposes of this sub-section, the word “subsidiary” shall include associate company and joint venture.

3. The provisions of this Act applicable to the preparation, adoption and audit of the financial statements of a holding company shall, mutatis mutandis, apply to the consolidated financial statements referred to in sub-section (3).

4. Without prejudice to sub-section (1), where the financial statements of a company do not comply with the accounting standards referred to in subsection (1), the company shall disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviation.

5. The Central Government may, on its own or on an application by a class or classes of companies, by notification19, exempt any class or classes of companies from complying with any of the requirements of this section or the rules made thereunder, if it is considered necessary to grant such exemption in the public interest and any such exemption may be granted either unconditionally or subject to such conditions as may be specified in the notification.

6. If a company contravenes the provisions of this section, the managing director, the whole-time director in charge of finance, the Chief Financial Officer or any other person charged by the Board with the duty of complying with the requirements of this section and in the absence of any of the officers mentioned above, all the directors shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

Explanation —For the purposes of this section, except where the context otherwise requires, any reference to the financial statement shall include any notes annexed to or forming part of such financial statement, giving information required to be given and allowed to be given in the form of such notes under this Act.

ACCOUNTING STANDARD (AS) 21 (ISSUED 2001)

Consolidated Financial Statements

[This Accounting Standard includes paragraphs set in bold italic type and plain type, which have equal authority. Paragraphs in bold italic type indicate the main principles. This Accounting Standard should be read in the context of its objective, the Preface to the Statements of Accounting Standards2 and the 'Applicability of Accounting Standards to Various Entities' (See Appendix 1 to this Compendium).]

Objective

The objective of this Standard is to lay down principles and procedures for preparation and presentation of consolidated financial statements. Consolidated financial statements are presented by a parent (also known as holding enterprise) to provide financial information about the economic activities of its group. These statements are intended to present financial information about a parent and its subsidiary(ies) as a single economic entity to show the economic resources controlled by the group, the obligations of the group and results the group achieves with its resources.

Scope

1. This Standard should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent.

2. This Standard should also be applied in accounting for investments in subsidiaries in the separate financial statements of a parent.

3. In the preparation of consolidated financial statements, other Accounting Standards also apply in the same manner as they apply to the separate financial statements.

4. This Standard does not deal with:

a) methods of accounting for amalgamations and their effects on consolidation, including goodwill arising on amalgamation (see AS 14, Accounting for Amalgamations);

b) accounting for investments in associates (at present governed by AS 13, Accounting for Investments3); and

c) accounting for investments in joint ventures (at present governed by AS 13, Accounting for Investments4).

Definitions

5. For the purpose of this Standard, the following terms are used with the meanings specified:

5.1 Control:

– the ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an enterprise; or

– control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.

5.2 A subsidiary is an enterprise that is controlled by another enterprise (known as the parent).

5.3 A parent is an enterprise that has one or more subsidiaries.

5.4 A group is a parent and all its subsidiaries.

5.5 Consolidated financial statements are the financial statements of a group presented as those of a single enterprise.

5.6 Equity is the residual interest in the assets of an enterprise after deducting all its liabilities.

5.7 Minority interest is that part of the net results of operations and of the net assets of a subsidiary attributable to interests, which are not owned, directly or indirectly through subsidiary (ies), by the parent.

6. Consolidated financial statements normally include consolidated balance sheet, consolidated statement of profit and loss, and notes, other statements and explanatory material that form an integral part thereof. Consolidated cash flow statement is presented in case a parent presents its own cash flow statement. The consolidated financial statements are presented, to the extent possible, in the same format as that adopted by the parent for its separate financial statements.

Explanation:

All the notes appearing in the separate financial statements of the parent enterprise and its subsidiaries need not be included in the notes to the consolidated financial statement. For preparing consolidated financial statements, the following principles may be observed in respect of notes and other explanatory material that form an integral part thereof:

– Notes which are necessary for presenting a true and fair view of the consolidated financial statements are included in the consolidated financial statements as an integral part thereof.

– Only the notes involving items which are material need to be disclosed. Materiality for this purpose is assessed in relation to the information contained in consolidated financial statements. In view of this, it is possible that certain notes which are disclosed in separate financial statements of a parent or a subsidiary would not be required to be disclosed in the consolidated financial statements when the test of materiality is applied in the context of consolidated financial statements.

– Additional statutory information disclosed in separate financial statements of the subsidiary and/or a parent having no bearing on the true and fair view of the consolidated financial statements need not be disclosed in the consolidated financial statements. An illustration of such information in the case of companies is attached to the Standard.

Presentation of Consolidated Financial Statements

7. A parent which presents consolidated financial statements should present these statements in addition to its separate financial statements.

8. Users of the financial statements of a parent are usually concerned with, and need to be informed about, the financial position and results of operations of not only the enterprise itself but also of the group as a whole.

This need is served by providing the users

– separate financial statements of the parent; and

– consolidated financial statements, which present financial information about the group as that of a single enterprise without regard to the legal boundaries of the separate legal entities.

Scope of Consolidated Financial Statements

9. A parent which presents consolidated financial statements should consolidate all subsidiaries, domestic as well as foreign, other than those referred to in paragraph 11.

10. The consolidated financial statements are prepared on the basis of financial statements of parent and all enterprises that are controlled by the parent, other than those subsidiaries excluded for the reasons set out in paragraph 11. Control exists when the parent owns, directly or indirectly through subsidiary(ies), more than one-half of the voting power of an enterprise. Control also exists when an enterprise controls the composition of the board of directors (in the case of a company) or of the corresponding governing body (in case of an enterprise not being a company) so as to obtain economic benefits from its activities. An enterprise may control the composition of the governing bodies of entities such as gratuity trust, provident fund trust etc. Since the objective of control over such entities is not to obtain economic benefits from their activities, these are not considered for the purpose of preparation of consolidated financial statements. For the purpose of this Standard, an enterprise is considered to control the composition of:

– the board of directors of a company, if it has the power, without the consent or concurrence of any other person, to appoint or remove all or a majority of directors of that company. An enterprise is deemed to have the power to appoint a director, if any of the following conditions is satisfied:

  a. a person cannot be appointed as director without the exercise in his favour by that enterprise of such a power as aforesaid; or

  b. a person's appointment as director follows necessarily from his appointment to a position held by him in that enterprise; or

  c. the director is nominated by that enterprise or a subsidiary thereof.

– the governing body of an enterprise that is not a company, if it has the power, without the consent or the concurrence of any other person, to appoint or remove all majority of members of the governing body of that other enterprise. An enterprise is deemed to have the power to appoint a member, if any of the following conditions is satisfied:

  a. a person cannot be appointed as member of the governing body without the exercise in his favour by that other enterprise of such a power as aforesaid; or

  b. a person's appointment as member of the governing body follows necessarily from his appointment to a position held by him in that other enterprise; or

  c. the member of the governing body is nominated by that other enterprise.

Explanation:

It is possible that an enterprise is controlled by two enterprises — one controls by virtue of ownership of majority of the voting power of that enterprise and other controls, by virtue of an agreement or otherwise, the composition of the board of directors so as to obtain economic benefit from its activities. In such a rare situation, when an enterprise is controlled by two enterprises as per the definition of 'control', the first mentioned enterprise will be considered as subsidiary of both the controlling enterprises within the meaning of this Standard and, therefore, both the enterprises need to consolidate the financial statements of that enterprise as per the requirements of this Standard.

11. A subsidiary should be excluded from consolidation when:

– control is intended to be temporary because the subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future; or

– it operates under severe long-term restrictions which significantly impair its ability to transfer funds to the parent. In consolidated financial statements, investments in such subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments. The reasons for not consolidating a subsidiary should be disclosed in the consolidated financial statements.

Explanation:

a. Where an enterprise owns majority of voting power by virtue of ownership of the shares of another enterprise and all the shares are held as 'stock-intrade' and are acquired and held exclusively with a view to their subsequent disposal in the near future, the control by the first mentioned enterprise is considered to be temporary within the meaning of paragraph 11(a).

b. The period of time, which is considered as near future for the purposes of this Standard primarily depends on the facts and circumstances of each case. However, ordinarily, the meaning of the words 'near future' is considered as not more than twelve months from acquisition of relevant investments unless a longer period can be justified on the basis of facts and circumstances of the case. The intention with regard to disposal of the relevant investment is considered at the time of acquisition of the investment. Accordingly, if the relevant investment is acquired without an intention to its subsequent disposal in near future, and subsequently, it is decided to dispose off the investments, such an investment is not excluded from consolidation, until the investment is actually disposed off. Conversely, if the relevant investment is acquired with an intention to its subsequent disposal in near future, but, due to some valid reasons, it could not be disposed off within that period, the same will continue to be excluded from consolidation, provided there is no change in the intention.

12. Exclusion of a subsidiary from consolidation on the ground that its business activities are dissimilar from those of the other enterprises within the group is not justified because better information is provided by consolidating such subsidiaries and disclosing additional information in the consolidated financial statements about the different business activities of subsidiaries. For example, the disclosures required by Accounting Standard (AS) 17, Segment Reporting, help to explain the significance of different business activities within the group.

Consolidation Procedures

13. In preparing consolidated financial statements, the financial statements of the parent and its subsidiaries should be combined on a line by line basis by adding together like items of assets, liabilities, income and expenses. In order that the consolidated financial statements present financial information about the group as that of a single enterprise, the following steps should be taken:

– the cost to the parent of its investment in each subsidiary and the parent's portion of equity of each subsidiary, at the date on which investment in each subsidiary is made, should be eliminated;

– any excess of the cost to the parent of its investment in a subsidiary over the parent's portion of equity of the subsidiary, at the date on which investment in the subsidiary is made, should be described as goodwill to be recognised as an asset in the consolidated financial statements;

- when the cost to the parent of its investment in a subsidiary is less than the parent's portion of equity of the subsidiary, at the date on which investment in the subsidiary is made, the difference should be treated as a capital reserve in the consolidated financial statements;
- minority interests in the net income of consolidated subsidiaries for the reporting period should be identified and adjusted against the income of the group in order to arrive at the net income attributable to the owners of the parent; and
- minority interests in the net assets of consolidated subsidiaries should be identified and presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders Minority interests in the net assets consist of:
    i. the amount of equity attributable to minorities at the date on which investment in a subsidiary is made; and
    ii. the minorities' share of movements in equity since the date the parent-subsidiary relationship came in existence.

Where the carrying amount of the investment in the subsidiary is different from its cost, the carrying amount is considered for the purpose of above computations.

Explanation:

- The tax expense (comprising current tax and deferred tax) to be shown in the consolidated financial statements should be the aggregate of the amounts of tax expense appearing in the separate financial statements of the parent and its subsidiaries.
- The parent's share in the post-acquisition reserves of a subsidiary, forming part of the corresponding reserves in the consolidated balance sheet, is not required to be disclosed separately in the consolidated balance sheet keeping in view the objective of consolidated financial statements to present financial information of the group as a whole. In view of this, the consolidated reserves disclosed in the consolidated balance sheet are inclusive of the parent's share in the post-acquisition reserves of a subsidiary.

14. The parent's portion of equity in a subsidiary, at the date on which investment is made, is determined on the basis of information contained in the financial statements of the subsidiary as on the date of investment. However, if thefinancial statements of a subsidiary, as on the date of investment, are not available and if it is impracticable to draw the financial statements of the subsidiary as on that date, financial statements of the subsidiary for the immediately preceding period are used as a basis for consolidation. Adjustments are made to these financial statements for the effects of significant transactions or other events that occur between the date of such financial statements and the date of investment in the subsidiary.

15. If an enterprise makes two or more investments in another enterprise at different dates and eventually obtains control of the other enterprise, the consolidated financial statements are presented only from the date on which holding-subsidiary relationship comes in existence. If two or more investments are made over a period of time, the equity of the subsidiary at the date of investment, for the purposes of paragraph 13 above, is generally determined on a step-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment.

16. Intragroup balances and intragroup transactions and resulting unrealised profits should be eliminated in full. Unrealised losses resulting from intragroup transactions should also be eliminated unless cost cannot be recovered.

17. Intragroup balances and intragroup transactions, including sales, expenses and dividends, are eliminated in full. Unrealised profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full. Unrealised losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered.

18. The financial statements used in the consolidation should be drawn up to the same reporting date. If it is not practicable to draw up the financial statements of one or more subsidiaries to such date and, accordingly, those financial statements are drawn up to different reporting dates, adjustments should be made for the effects of significant transactions or other events that occur between those dates and the date of the parent's financial statements. In any case, the difference between reporting dates should not be more than six months.

19. The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements are usually drawn up to the same date. When the reporting dates are different, the subsidiary often prepares, for consolidation purposes, statements as at the same date as that of the parent. When it is impracticable to do this, financial statements drawn up to different reporting dates may be used provided the difference in reporting dates is not more than six months. The consistency principle requires that the length of the reporting periods and any difference in the reporting dates should be the same from period to period.

20. Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

21. If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements when they are used in preparing the consolidated financial statements.

22. The results of operations of a subsidiary are included in the consolidated financial statements as from the date on which parent-subsidiary relationship came in existence. The results of operations of a subsidiary with which parent-subsidiary relationship ceases to exist are included in the consolidated statement of profit and loss until the date of cessation of the relationship. The difference between the proceeds from the disposal of investment in a subsidiary and the carrying amount of its assets less liabilities as of the date of disposal is recognised in the consolidated statement of profit and loss as the profit or loss on the disposal of the investment in the subsidiary. In order to ensure the comparability of the financial statements from one accounting period to the next, supplementary information is often provided about the effect of the acquisition and disposal of subsidiaries on the financial position at the reporting date and the results for the reporting period and on the corresponding amounts for the preceding period.

23. An investment in an enterprise should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments, from the date that the enterprise ceases to be a subsidiary and does not become an associate.

24. The carrying amount of the investment at the date that it ceases to be a subsidiary is regarded as cost thereafter.

25. Minority interests should be presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders. Minority interests in the income of the group should also be separately presented.

26. The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.

27. If a subsidiary has outstanding cumulative preference shares which are held outside the group, the parent computes its share of profits or losses after adjusting for the subsidiary's preference dividends, whether or not dividends have been declared.

Accounting for Investments in Subsidiaries in a Parent's Separate Financial Statements

28. In a parent's separate financial statements, investments in subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments.

Disclosure

29. In addition to disclosures required by paragraph 11 and 20, following disclosures should be made:

– in consolidated financial statements a list of all subsidiaries including the name, country of incorporation or residence, proportion of ownership interest and, if different, proportion of voting power held;

– in consolidated financial statements, where applicable:

i. the nature of the relationship between the parent and a subsidiary, if the parent does not own, directly or indirectly through subsidiaries, more than one-half of the voting power of the subsidiary;

ii. the effect of the acquisition and disposal of subsidiaries on the financial position at the reporting date, the results for the reporting period and on the corresponding amounts for the preceding period; and

iii. the names of the subsidiary(ies) of which reporting date(s) is/ are different from that of the parent and the difference in reporting dates.

Transitional Provisions

30. On the first occasion that consolidated financial statements are presented, comparative figures for the previous period need not be presented. In all subsequent years full comparative figures for the previous period should be presented in the consolidated financial statements.

In the case of companies, the information such as the following given in the notes to the separate financial statements of the parent and/or the subsidiary need not be included in the consolidated financial statements:

– Source from which bonus shares are issued, e.g., capitalization of profits or Reserves or from Share Premium Account.

– Disclosure of all unutilised monies out of the issue indicating the form in which such unutilised funds have been invested.

– The name(s) of small scale industrial undertaking(s) to whom the company owe any sum together with interest outstanding for more than thirty days.

– A statement of investments (whether shown under “Investment” or under “Current Assets” as stock-in-trade) separately classifying trade investments and other investments, showing the names of the bodies corporate (indicating separately the names of the bodies corporate under the same management) in whose shares or debentures, investments have been made (including all investments, whether existing or not, made subsequent to the date as at which the previous balance sheet was made out) and the nature and extent of the investment so made in each such body corporate.

– Quantitative information in respect of sales, raw materials consumed, opening and closing stocks of goods produced/traded and purchases made, wherever applicable.

– A statement showing the computation of net profits in accordance with section 349 of the Companies Act, 1956, with relevant details of the calculation of the commissions payable by way of percentage of such profits to the directors (including managing directors) or manager (if any).

– In the case of manufacturing companies, quantitative information in regard to the licensed capacity (where licence is in force); the installed capacity; and the actual production.

– Value of imports calculated on C.I.F. basis by the company during the financial year in respect of :

  a. raw materials;

  b. components and spare parts;

  c. capital goods.

– Expenditure in foreign currency during the financial year on account of royalty, know-how, professional, consultation fees, interest, and other matters.

– Value of all imported raw materials, spare parts and components consumed during the financial year and the value of all indigenous raw materials, spare parts and components similarly consumed and the percentage of each to the total consumption.

– The amount remitted during the year in foreign currencies on account of dividends, with a specific mention of the number of non-resident shareholders, the number of shares held by them on which the dividends were due and the year to which the dividends related.

– Earnings in foreign exchange classified under the following heads, namely:

  a. export of goods calculated on F.O.B. basis;

  b. royalty, know-how, professional and consultation fees;

  c. interest and dividend;

  d. other income, indicating the nature thereof.

TAXATION OF IMMOVABLE PROPERTY RECEIVED AS DONATION

1. INTRODUCTION

1.1 In case of a charitable or religious organization immovable property received as donation is also part of the income or corpus donation received by such organisations. There has been considerable confusion regarding the treatment of such donation in kind in the Books of Accounts and also for taxation purposes.

1.2 Any immovable property received by an organisation should not be treated as income and shall not be subject to 85% application as is required under the Income Tax Laws. It may be noted that under the prevailing Income Tax laws a charitable or religious organisation is required to apply at least 85% of its income every year. The problem with an immovable property is that it is not available for application in the year of receipt. In other words, an immovable property cannot be applied, accumulated or invested. Therefore, it is not possible to show 85% application against such income.

1.3 The CBDT has also issued a circular in this regard. Further there is considerable judicial precedence available to establish that a donation of immovable property is not subject to 85% application at the hands of the recipient organisation.

2. DONATION OF IMMOVABLE PROPERTY SHOULD BE TREATED AS CORPUS DONATION

2.1 In case of a charitable or religious organization immovable property received as donation is treated as corpus donation. As a matter of fact even funds received towards construction of building are also treated as corpus donation. In the case of *St. Anns Home for the Aged v. ITO* [1982] 13 TTJ (Bang.) 185, it has been held that the voluntary contributions expressly received for construction of a building were corpus donations, since they were received and utilized for a capital purpose. In the case of *ITO v. Satya Kabir Sahabani Gadi* [1994] 50 TTJ (Ahd.) 501, the Tribunal held that Building Fund and Kayami Fund were corpus of the Trust and donations received towards such funds were corpus donations. In this case it was held that receipts from a drama staged for the purpose of construction of a new building formed is corpus donation. The Tribunal was of the view that the occasion and circumstances of the case effectively implied that the donations were specifically given for the purpose of construction of a new building.

2.2 Secondly, any donation received in kind is not available for utlisation or accumulation unless a further inter charity donation is made, therefore it has been held that such receipts are not subject to application. The only requirement is that they should be used for charitable/religious purposes.

3. CBDT CIRCULAR NO. 580, DATED 14-9-1990

3.1 There is a CBDT Circular No. 580, dated 14-9-1990, which clarifies that donation in kind other than jewellery and furniture (which are specifically exempted) are not subject to application. The Circular is reproduced as under:

"134. Where donations in kind are not in form of jewellery, furniture or any other notified article

– Under section 10(23C)(iv) and (v) of the Income-tax Act, income received by certain charitable and religious funds, trusts and institutions is exempt from tax if the conditions specified for this purpose are satisfied. One such condition, as laid down in the third proviso to section 10(23C), is that the fund, trust or institution applies its income, or accumulates it for application, wholly and exclusively to the object for which it is established and it does not invest or deposit its funds (other than voluntary contributions received and maintained in the form of jewellery, furniture or any other article as the Board may, by notification in the Official Gazette specify) for any period during the previous year otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11 of the Income-tax Act.

– References have been received from various trusts and institutions pointing out that certain funds, trusts and institutions running hospitals, creches, orphanages, schools, etc., and enjoying exemption under section 10(23C)(iv) or (v), of the Income-tax Act, often receive donations in kind from various sources for application towards their charitable purposes. These contributions may be in the shape of books, clothes for the poor, grains to feed the poor, drugs, hospital equipment, etc. It has been pointed out that all these are used as such for the purposes of the fund, trust or institution.

– A doubt has, however, been raised as to whether the fund, trust or institution would be eligible for the tax exemption under section 10(23C)(iv) or (v) of the Act even if the donations-in-kind are not in the form of jewellery, furniture or any other article notified by the Board for the purposes of these provisions.

– Since the donations-in-kind, of the nature referred to above, received by a fund, trust or institution, would be income within the meaning of section 2(24) of the Income-tax Act, it is clarified that use of these towards objects for which the fund, trust or institution is established would be regarded as application of income of the fund, trust or institution within the meaning of clause (a) of the third proviso to section 10(23C). Accordingly, the fund, trust or institution would be eligible for the tax exemption if the other conditions specified in section 10 (23C)(iv) of the Income-tax Act are satisfied."

4. RULING OF THE JODHPUR TRIBUNAL WITH REGARD TO IMMOVABLE PROPERTY

4.1 The Jodhpur Tribunal in the case the I.T.O., Ward 2(2), Jodhpur Vs. Shri Sachyaya Mataji Trust, Jodhpur, I.T.A. No.538/Jodh/2013 for Assessment Year: 2009-10 with regard to the issue of immovable properties received as donation, held as under:

4.2 "17. We have considered the submissions of both the parties and carefully gone through the material available on the record. In the present case, it is an admitted fact that the assessee received the donations in kind and the same could not be applied, accumulated or invested, therefore, it cannot be treated as income. Therefore, the Ld. CIT(A) was fully justified in reversing the observations of the Assessing Officer. We do not see any infirmity in the order of the Ld. CIT(A) on this issue."

SUPREME COURT RULING ON TREATMENT OF INTEREST ON CORPUS FUND

1. OVERVIEW

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

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.

1.3 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.

1.4 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.

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

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.

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.

3. LANDMARK RULING BY SUPREME COURT ON INTEREST EARNED ON CORPUS FUND

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.

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.

4. IMPORTANT CASES REGARDING NON-TAXABILITY OF CORPUS DONATION

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.

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 :

– 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.

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

– The voluntary contributions received by the assesse towards the corpus cannot be brought to tax.'

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 bedeemed 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:-

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

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

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

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

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

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

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

5. THE LEGISLATIVE INTENT OF TREATING CORPUS DONATION AS INCOME

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***.

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.

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 assesse trust cannot be brought to tax despite the fact that the assesse-trust was not registered u/s 12A/12AA of the Act.

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:

- Direction that donation should form part of corpus should come from the donor and not the discretion of others.
- It does not depend on the sweet will of the donee/institution or other agencies.
- 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 Incometax, 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.'

5.5 The following decisions are also relevant:

- ITO v. Smt. Basanti Devi & Shri Chakhan Lal Garg Education Trust, ITA No. 5082/Del./2010 date 19.1.2011, Delhi Tribunal.
- 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.

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 subclause(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;]

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

(vd) 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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BRANCH OFFICE AND LIAISON OFFICE NOW UNDER FCRA

1. INTRODUCTION

1.1 The Foreign Exchange Management Act (FEMA), 1999 regulates the establishment of Branch Office/Liaison Office/Project Office India by foreign entities and foreign donor agencies.

The Foreign Exchange Management (Establishment of Branch Office or Liaison Office or Project Office or any other place of Business) Regulation 2016 vide G.S.R 384 dated 31.03.2016 hitherto was the Statutory Regulation. It should be read with Notification No. FEMA 22(R)/2016-RB dated March 31, 2016, by virtue of which all international NGOs are required to seek permission from the RBI.

In other words the establishment and activities of Branch and Liaison Offices is regulated by RBI under FEMA.

2. RECENT AMENDMENT

2.1 Recently, the Reserve Bank of India' has issued an amended notification dated 31st August 2018; this notification requires that any foreign entity engaged in any activity, partly or wholly, covered under Foreign Contribution (Regulation) Act, 2010 (FCRA), shall obtain a certificate of registration under FCRA and shall not seek permission under FEMA. The notification is enclosed in ***Annexure 1.***

2.2 INGOs or International Donor Agencies seeking registration under FEMA will now be required to apply to MHA under FCRA 2010 if they have any activities which come under the purview of FCRA 2010. In other words, all agencies engaged in charitable activity either directly or indirectly, in India, will have to obtain FCRA registration or prior permission for their existence in India.

2.3 The agencies which are allowed to continue the existing Liaison Office and Branch Office status should not have any activity covered within the purview of FCRA 2010. All new application to Reserve Bank of India regarding Liaison Office and Branch Office should come with a declaration in Form FNC as under:

"We will not undertake either partly or fully, any activity that is covered under Foreign Contribution Regulation Act, 2010 (FCRA) and we understand that any misrepresentation made or false information furnished by us in this behalf would render the approval granted under the Foreign Exchange Management (Establishment in India of a branch office or liaison office or a project office or any other place of business) Regulations, 2016, automatically as void ab initio (Latin for 'from the beginning') and such approval by the Reserve Bank shall stand withdrawn without any further notice"

2.4 This amendment is abrupt and sudden and shall have very wide implications and repercussions, some such issues are discussed herein.

3. WHETHER IT HAS ANY IMPACT ON THE EXISTING LO/BRANCH?

3.1 There is no formal withdrawal of the approval/registration provided to the existing Liaison Office and Branch Office, however the revision in the Form FNC states that any approval granted to BO or LO will be treated as void ab initio (Latin for 'from the beginning') which implies that any organisation having any activity falling within the purview of FCRA 2010 cannot continue without obtaining registration from FCRA Department.

3.2 All existing Branch Office and Liaison Office should apply to the FCRA Department for regularisation of their existence in India.

4. WHAT SHALL BE THE MEANING OF ACTIVITIES COVERED UNDER FCRA 2010?

4.1 There is no specific definition of 'activities' under FCRA 2010, moreover FCRA 2010 is about activities carried out of Foreign Contribution. In other words FCRA applies only if foreign contribution is received by Indian Citizens or entities working in India. The FCRA 2010 doesnot apply to foreign entities at all unless they receive contribution from sources other than headquarter. In other words if a Branch Office of a foreign entity receives funds from its headquarter, such receipts cannot be treated as foreign contribution. In that sense this notification is not consistent with the FCRA Law and legally it can be challenged, because FCRA can regulate only if foreign contribution is received, it cannot regulate activities irrespective of source.

4.2 Further, FCRA covers all activities made out of foreign contribution, therefore the issue is whether such BO/LO are in possession of foreign contribution or not. If such BO and LO are receiving only inward remitances from their headquarter then they are not covered under FCRA.

4.3 The RBI could have easily put restrictions on all existing BO and LO by not allowing them to either do any kind of charitable activity or raise funds in that regard, in India.

5. WHAT IF A FOREIGN BRANCH IS HAVING INCOME FROM ONLY INDIAN SOURCES

5.1 There are many branches of foreign entities particularly international NGOs which have 12AA registration under the Income Tax Act (this registration provides tax exemptions to NGOs against income generated in India). Such branches have considerable income from Indian sources which is applied for charitable purposes.

5.2 In our opinion such BOs will also get affected with this notification and will have to apply to the FCRA department for continuation of their activities in India. In other words, activities of BO and LO will get attracted under this provision irrespective of the source of income.

6. OTHER ISSUES

6.1 It is not known how FCRA will regulate activities of such organisation when such activities could be out of both local and foreign sources.

6.2 Under FCRA law all FC contribution is required to be received in a designated bank account. It is not known how a designated bank account could be maintained for a BO of a foreign entity because neither the inward remittance could be treated as foreign contribution nor the Indian income could be treated as foreign contribution.

6.3 There are some BO/LO who do not have any taxable income in India or registration in India. In such cases it is not clear how they will fulfill the registration formalities regarding document of registration or PAN number etc.

Annexure-1

Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) (Amendment) Regulations, 2018

RESERVE BANK OF INDIA
(Foreign Exchange Department)
(CENTRAL OFFICE)

NOTIFICATION

Mumbai, the 31st August, 2018

No. FEMA 22(R) (1)/2018-RB

Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) (Amendment) Regulations, 2018

G.S.R. 827(E).— In exercise of the powers conferred by sub-section (6) of Section 6 of the **Foreign Exchange Management Act, 1999** (42 of 1999), the Reserve Bank makes the following amendments to the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016, Notification No. FEMA 22(R)/2016-RB dated March 31, 2016, namely:

1. **Short Title and Commencement: –**

    i. These regulations may be called the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) (Amendment) Regulations, 2018.

    ii. These regulations shall come into force from the date of their publication in the Official Gazette.

2. **Amendment to Regulation 5:**

    In the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016 (Notification No. FEMA 22(R)/2016-RB dated March 31, 2016), in the Regulation 5,

    (A) The existing sub-regulation d. shall be substituted by the following namely:

    d. the applicant is a Non-Government Organisation, Non-Profit Organisation, Body/Agency/Department of a foreign government. However, if such entity is engaged, partly or wholly, in any of the activities covered under Foreign Contribution (Regulation) Act, 2010 (FCRA), they shall obtain a certificate of registration under the said Act and shall not seek permission under this regulation.

3. **Amendment to Form FNC (Annex C):**

    In the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016

(Notification No. FEMA 22(R)/2016-RB dated March 31, 2016), in the existing form FNC (Annex C), in Part –II, under the heading 'Declaration', in clause (ii), at the end of the existing sentence, the following shall be added, namely:

" We will not undertake either partly or fully, any activity that is covered under Foreign Contribution Regulation Act, 2010 (FCRA) and we understand that any misrepresentation made or false information furnished by us in this behalf would render the approval granted under the Foreign Exchange Management (Establishment in India of a branch office or liaison office or a project office or any other place of business) Regulations, 2016, automatically as void ab initio and such approval by the Reserve Bank shall stand withdrawn without any further notice".

[F.No. 16/13/EM/2014-Part-I]
R. K. MOOLCHANDANI,
Chief General Manager

Foot Note:- *The Principal Regulations were published in the Official Gazette vide* ***G.S.R. No.384 (E) dated March 31, 2016*** *in Part II, Section 3, sub-Section (i).*

RECENT CIRCULAR ON CUSTODY OF FC ASSETS BY CENTRAL GOVERNMENT

1. OVERVIEW OF THE PROVISIONS PERTAINING TO MANAGEMENT OF FC ASSETS

1.1 Recently the Central Government, Ministry of Home Affairs has issued a notification dt. 05.11.2018 wherein it has been notified that the Additional Chief Secretary or Principal Secretary (Home) of the concerned State Government or Union Territory (where the assets of the person whose registration has been cancelled under section 14 of the said Act are physically located), as competent authority for the purposes of section 15 of the said Act. The copy of the notification is enclosed in *Annexure 1*.

1.2 As per section 15 of Foreign Contribution Regulation Act (FCRA), 2010 the Central Government retains the right to manage the properties in case of cancellation of FC registration. The Competent Authority mentioned in that circular was not defined so far. This notification just defines the competent authority. It does not entail any new direction regarding managing FC properties or confiscation of FC property.

1.3 It may also be noted that Section 15 of FCRA, 2010 provides limited power to the competent authority (restricted only to management of the property for charitable purposes). The competent authority is required to return the foreign contribution or foreign assets back to the FC registered organisation once the FC registration is restored.

1.4 The Competent Authority on directions of the Central Government can manage the activities for such period and in such manner as may be directed. The Competent Authority also has the authority to dispose of assets only for the purposes of running the activities. In other words, cancellation of FCRA per se does not empower the competent authority to confiscate the properties. The properties may be taken over to continue that activity. This provision is apparently not practical and realistic.

1.5 The Competent Authority shall be state specific. In other words, if an NGO is working and having assets in various states of India, then the Competent Authority will be the authority of that particular state in which the assets physically exist.

1.6 In case of assets built out of both FC and domestic funds, the competent authority will have the right only to the extent of the FC portion of the assets.

2. MANAGEMENT OF FOREIGN CONTRIBUTION AND ASSETS AFTER CANCELLATION OF REGISTRATION

2.1 Under section 15 of the FCRA 2011, it is provided that the custody of foreign contribution or assets of any organisation or person whose certificate has been cancelled shall vest in such authority as may be prescribed. In other words, once the registration certificate is cancelled, the Central Government reserves the right to determine the authority and manner in which the foreign contribution and foreign assets shall be kept and managed. The text of section 15(1) is as under:

15.(1) The foreign contribution and assets created out of the foreign contribution in the custody of every person whose certificate has been cancelled under section 14 shall vest in such authority as may be prescribed.

(2) The authority referred to in sub-section (1) may, if it considers necessary and in public interest, manage the activities of the person referred to in that sub-section for such period and in such manner, as the Central Government may direct and such authority may utilise the foreign contribution or dispose of the assets created out of it in case adequate funds are not available for running such activity.

(3) The authority referred to in sub-section (1) shall return the foreign contribution and the assets vested upon it under that sub-section to the person referred to in the said subsection if such person is subsequently registered under this Act."

2.2 Further, as per Rule 15 of FCRR 2011 the bank balance available in the designated bank account shall remain in the custody of the respective bank after the cancellation Bof FC certificate. The text of the Rule is reproduced as under:

15. Custody of foreign contribution in respect of a person whose certificate has been cancelled - (1) The amount of foreign contribution lying unutilised in the exclusive foreign contribution bank account of a person whose certificate of registration has been cancelled shall vest with the banking authority concerned till the Central Government issues further directions in the matter.

(2) If a person whose certificate of registration has been cancelled transfers/ has transferred the foreign contribution to any other person, the provisions of sub-rule (1) of this rule shall apply to the person to whom the fund has been transferred."

2.3 In the event of cancellation of the FCRA registration, the Central Government may exercise that the following powers :

– The Central Government reserves the right to take over or determine the manner in which the asset shall be managed or preserved.

– In the absence of any limitation, the power to take over or manage FC funds and FC assets shall apply to all the FC assets and balances accumulated since 1976 i.e. the applicability of the FCRA 1976.

– The Central Government reserves the right to dispose of the assets or utilise the funds during the cancellation period.

– The Central Government shall return all the assets and fund if the FC registration is restored.

– At the time of the cancellation of FC registration, the bank balance available in the designated bank account shall automatically remain in the custody of the respective bank and the organisation cannot use it. The funds available in the designated bank account can only be used as per any further directions from the Central Government. It may be noted that Rule 15 of FCRR 2011 only talks about the bank balance in the designated bank account. Therefore any fund available in other bank accounts or FDRs shall not remain in the custody of the bank. However, the Central Government shall have the right to issue direction over the use and management of such funds also.

3. CAN THE COMPETENT AUTHORITY CONFISCATE THE ASSETS OF ORGANISATIONS WHOSE REGISTRATION IS CANCELLED

3.1 There is nothing in the law to suggest that the assets of the organisations, whose registration is cancelled, can be confiscated. In fact, there is no provision of confiscation by the competent authority, unless there is prosecution and conviction under any provision of FCRA. The Competent Authority is only empowered to manage the assets for a specific period of time and then has to return the assets. However, Section 15 also provides that the competent authority may sale the assets for advancement of the objectives of the concerned NGO- any sale of assets can only happen if the competent authority is running the activities which looks unlikely and impractical.

3.2 In other words, there is no substantive power with the competent authority to arbitrarily take away the assets.

4. WHAT ABOUT NGOS HAVING ASSETS IN VARIOUS STATES OF THE COUNTRY

4.1 The Competent Authority will be different for each state as notified in the enclosed notification, therefore, an NGOs having India wide operation shall be subject to the competent authority of all the states in which it is physically functioning.

5. MANAGEMENT OF FOREIGN CONTRIBUTION AND ASSETS AFTER DISSOLUTION

5.1 Under section 22 of the FCRA 2010, it is provided that the custody of foreign contribution or assets of any organisation or person which has been dissolved shall vest in such authority as may be prescribed. In other words, once the organisation is dissolved or ceases to exist, then the Central Government reserves the right to determine the authority and manner in which the foreign contribution and foreign assets shall be kept and managed. The text of section 22 is as under :

"22. Where any person who was permitted to accept foreign contribution under this Act, ceases to exist or has become defunct, all the assets of such person shall be disposed off in accordance with the provisions contained in any law for the time being in force under which the person was registered or incorporated, and in the absence of any such law, the Central Government may, having regard to the nature of assets created out of foreign contribution received under this Act, by notification, specify that all such assets shall be disposed off by such authority, as it may specify, in such manner and procedure as may be prescribed."

5.2 In the event of cancellation of the FCRA registration, the Central Government will have the following powers :

– The right to take over or determine the manner in which the asset shall be disposed of.

– The power to take over or manage FC funds and FC assets. Such power shall apply to all the FC assets and balances accumulated since 1976 i.e. the applicability of the FCRA 1976.

भारत का राजपत्र
The Gazette of India

असाधारण
EXTRAORDINARY
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PART II—Section 3—Sub-section (ii)
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गृह मंत्रालय
अधिसूचना
नई दिल्ली, 5 नवम्बर, 2018

का.आ. 5650(अ).—केंद्रीय सरकार, विदेशी अभिदाय (विनियमन) अधिनियम, 2010 (2010 का 42) [illegible] की धारा 15 की उपधारा (1) [illegible] की धारा 14 के अधीन [illegible] की धारा 15 के प्रयोजनों के लिए सक्षम प्राधिकारी के रूप में [illegible]।

[फा. सं. II/21022/23(43)/2018-एफसीआरए-III]
[illegible], संयुक्त सचिव

MINISTRY OF HOME AFFAIRS
NOTIFICATION
New Delhi, the 5th November, 2018

S.O. 5650(E).—In exercise of the power conferred by sub-section (1) of section 15 of the Foreign Contribution (Regulation) Act, 2010 (42 of 2010) (herein after referred to as the said Act), the Central Government hereby prescribes the Additional Chief Secretary or Principal Secretary (Home) of the concerned State Government or Union territory (where the assets of the person whose registration has been cancelled under section 14 of the said Act are physically located), as competent authority for the purposes of section 15 of the said Act.

[F. No. II/21022/23(43)/2018-FCRA-III]
ANIL MALIK, Jt. Secy.

[illegible]
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and Published by the Controller of Publications, Delhi-110054.
MANOJ KUMAR VERMA

BELATED SUBMISSION OF AUDIT REPORT IN FORM 10B ALONGWITH IT RETURN

1. SUMMARY

1.1 Section 12A states various conditions for availing the exemption under the Act – the first condition is regarding application for registration under section 12AA and among the other conditions there is the requirement of audit by an Chartered Accountant as defined in the Explanation to sub-section (2) of section 288. The Audit Report is required to be prepared in Form 10B. It may be noted that prior to 2013-14 the Audit Report was submitted in hard copies. However, with effect from Assessment year 2013-14, it has become mandatory to upload online audit report in Form 10B.

1.2 As Online Filing of Audit Report in Form 10B has become mandatory along with the Income Tax Return, there have been litigations where the Assessing Officer has denied the benefit of tax exemptions under section 11 for delayed filing of Audit Report.

1.3 There are several cases where Form 10B was uploaded after the submission of Return of Income and in such cases returns are processed without giving benefit of sec. 11 of the Income Tax Act,1961. In other words the total income was subjected to tax without providing any benefit under section 11.

1.4 In this issue we will try to understand the implications of delay in filing of Audit Report under Form 10B. In our opinion, as explained herein under, a delay in filing of Form 10B cannot result in any coercive action by the AO including withdrawal of exemptions under section 11.

2. THE CONDITIONS FOR AVAILING BENEFIT UNDER SECTION 11 AND 12

2.1 Section 12AA of the Income Tax Act provides conditions for applicability for Sec. 11 & 12 of the Income Tax Act,1961. The conditions are :

- The organisation/institution has to be registered u/s. 12AA of the Income Tax Act, 1961.
- If the organisation has adopted or undertaken modifications of the objects which do not conform to the conditions of registration, then within a period of thirty days from the date of said adoption or modification, application for approval of such modification to be submitted to the Principal Commissioner or Commissioner. (w.e.f. Asst Year 2018-19).
- The Trust or institution should get the accounts audited as required under the Act and shall submit the Audit Report in form no 10B along with the Return of income for the relevant Assessment Year.
- The organisation has to furnish the return of income in ITR-7 for the previous year under sub-section (4A) of sec 139, within the time allowed under that section (w.e.f. Asst Year 2018-19). In other words, delay in filing of return is also not permissible.

2.2 In the light of the above conditions it is mandatory to furnish Form 10B along with return of income as it is one of the conditions to claim the benefit u/s. 11 & 12.

3. FILING OF AUDIT REPORT ALONG WITH RETURN IS DIRECTORY AND NOT MANDATORY

3.1 In our opinion the requirement of submission of Form 10B along with the return though is one of the conditions for claiming the benefit of Sec. 11 & 12, it is directory in nature and not mandatory. In other words, it is a curable defect and the AO should accept belated filing of Audit Report in Form10B.

3.2 If the Audit Report is not submitted with the Income Tax Return, then such return should be treated as defective and a notice u/s. 139(9) should be given to rectify the defect/ deficiency in the return being submitted.The Audit report in Form 10B can also be submitted along with the revised return.

4. CBDT CIRCULAR REGARDING DELAYED FILING OF AUDIT REPORT

4.1 The Central Board of Direct Taxes(CBDT) has also issued the following circular clarifying the above issue, which is as follows:

(1/1148-CBDT F. No. 267/482/77-IT (Part) dated February 9, 1978—CBDT Bulletin Tech. XXIII/582.) :

"Charitable trust-Requirement of filing audit report in Form 10B—Section 12A(b)—Instructions regarding.—The Board have considered whether the requirement under Section 12A(b) of filing audit report 'along with the return of income' is mandatory so as to disentitle the trust from claiming exemption under Sections 11 and 12 in case of omission to furnish such report in the prescribed form along with the return.

Normally, it should be possible for a charitable or religious trust or institution to file the auditor's report along with the return of total income, where such trust or institution claims exemption under Sections 11 and 12. However, in cases where for reasons beyond the control of the assesse some delay has occurred in filing the said report the exemption as available to such trust under Sections 11 and 12 may not be denied merely on account of delay in furnishing the auditor's report and the Income-tax Officer should record reasons for accepting a belated audit report."

4.2 It may be noted that despite the CBDT circular indicating that the provisions related with the requirement of audit are directory and not mandatory, the assessee does not have any implied right to file belated audit reports. Audit reports are required and should be filed alongwith the return only. However, any delay in filing of Form 10B would not necessarily result in denial of exemptions under section 11.

5. CASE LAWS REGARDING DELAYED FILING OF AUDIT REPORT

5.1 In the case of CIT vs. Rai Bahadur Bissesswarlal Motilal Malwasie Trust (1992) 195 ITR 825, the Calcutta High Court has affirmed that that the requirement of filing the audit report with the return is merely a procedural requirement, and that exemption cannot be denied so long as the report is available to the assessing officer before the completion of assessment.

5.2 In the case of *Calcutta Management Association vs. ITO* (1992) 42 ITD 62, the Calcutta bench of the Tribunal held that the Audit Report can even be filed at the time of appeal before the Commissioner (Appeals).

5.3 A similar view has been taken by the Tribunal, in the case of *Swajan Pariwar Trust vs. ADIT(E)* (1997) 57 TTJ (Mum) (SMC) 77, that, where the trust filed the audit report along with a rectification application under section 154, it was entitled to the exemption, as the defect had been removed.

5.4 The Gujarat High Court in CIT v. Gujarat Oil & Allied Industries [1993] 201 ITR 325 (Guj.) held that the provision about furnishing of the auditor's report along with the return has to be treated as procedural provision and, therefore, directory in nature.

5.5 In the case National Horticulture Board v. CCIT [2009] 176 TAXMAN 167 (PUNJ. & HAR.) the Chief Commissioner dismissed application for approval under section 10(23C)(iv) on ground that audit reports in Form No. 10BB were not filed with returns and same were filed later, but were not dated as required under 10th proviso to said provision. The High Court held that provisions of the law having been substantially complied with, audit report should have been taken into account even if, strictly speaking, it was not filed with return and not in Form No. 10BB but in Form No. 10B as stated in impugned order.

5.6 The High Court of Calcutta CIT vs. Hardeodas Agarwala Trust (1992) 198 ITR 511 (Cal). held that whether a provision is directory or mandatory has to be considered in the context in which the conditions are imposed. Whether a statute is mandatory or directory depends on the intent of legislature and upon the language in which the intent is clothed. The meaning and intention of Legislature must govern and these are to be ascertained not only from the phraseology of the provision but also by considering its nature, its design, and the consequences which would follow from construing it one way or the other.

6. THE AUDIT REPORT CAN EVEN BE SUBMITTED AT THE APPELLATE STAGE

6.1 In the case CIT vs. Shahzedanand Charity Trust – (1997) 228 ITR 292 (PH), it has been clarified that the exemption available to the trust under section 11 may not be denied merely on account of delay in furnishing the auditor's report. The word 'shall' occurring in section 12A cannot, under the circumstances, be read as a 'must' making it mandatory for the trust to furnish the auditor's report along with the return. If for certain unavoidable circumstances, the assessee is unable to furnish the auditor's report along with the return, then the same can be furnished at a later date with the permission of the Assessing Officer, who may permit the assessee to do so after recording the reasons for so doing.

6.2 There was no merit in the submission of the revenue that, as per that circular, the auditor's report could only be furnished up to the stage of framing of the assessment as the power to condone the delay for accepting the auditor's report at a later date has only been given to the ITO and not thereafter, i.e., at the appellate stage. The CBDT, by issuing the above circular, has treated the provisions regarding furnishing of auditor's report along with the return to be procedural and, therefore, directory in nature. By showing sufficient cause, the auditor's report can be produced at any later stage either before the ITO or before the appellate authority.

7. CONCLUDING REMARK

7.1 To sum up, in our opinion if the Form 10B is not uploaded along with the return, such defect itself cannot result in denial of exemptions under section 11. Therefore, where return has been processed u/s. 143(1) denying the exemption u/s. 11 mainly on the ground that Form 10B was not uploaded with the return but filed subsequently, the concerned NGO should submit application to the assessing officer for condonation of delay for late submission of Form 10B along with the return of income and also the petition u/s 154 of the Income Tax Act,1961 for revising the intimation by allowing the benefit of section 11 of the Income Tax Act,1961.

Annexure 1

CBDT CIRCULAR CONDONATION OF DELAY FOR FORM NO. 10 AND FORM NO. 9A UNDER SECTION 119(2)(B)

Circular No. 7 / 2018

F.No.197/55/2018-ITA-I
Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes
North Block, New Delhi

20th December, 2018

Sub: Condonation of delay under section 119(2)(b) of the Income-tax Act, 1961 in filing of Form no. 10 and Form No. 9A for AY 2016-17

1. Under the provisions of section 11 of the Income-tax Act, 1961 (hereafter Act') the primary condition for grant of exemption to trust or institution in respect of income derived from property held under such trust is that the income derived from property held under trust should be applied for the charitable purposes in India. Where such income cannot be applied during the previous year, it has to be accumulated and applied for such purposes in accordance with various conditions provided in the section.
2. The Finance Act, 2015 amended section 11 and section 13 of the Act with effect from 01.04.2016 (A.Y. 2016-17). Consequently, Income-tax Rules, 1962 (hereafter 'Rules') were also amended vide the Income-tax (1st Amendment) Rules, 2016. As per the amended provisions of the Act read with rule 17 of the Rules, while 15% of the income can be accumulated indefinitely by the trust or institution, 85% of income can only be accumulated for a period not exceeding 5 years subject to the conditions, inter alia, that such person submits the prescribed Form No. 10 electronically to the Assessing Officer within the due date specified under section 139(1) of the Act.
3. Further, where the income from the property held under trust and applied to charitable or religious purposes falls short of 85% of the income derived during the previous year for the reason that the income has not been received during that year or any other reason, then on exercise of the option by submitting in Form No.9A electronically by the trust/institution on or before the due date of furnishing the return of income, such income shall be deemed to have been applied for charitable or religious purpose.
4. Representations have been received by the Board/ field authorities stating that the Form No. 9A and Form No.10 could not be filed in the specified time for AY 2016-17, which was the first year of e-filing of these forms. It has been requested that the delay in filing of Form No. 9A and Form No. 10 for AY 2016-17 may be condoned under section 119(2) (b) of the Act.
5. Accordingly, in supersession of earlier Circular/Instruction issued in this regard, with a view to expedite the disposal of applications filed by trusts for condoning the delay and in exercise of the powers conferred under section 119(2)(b) of the Act, the Central

Board of Direct Taxes hereby authorizes the Commissioners of Incometax, to admit belated applications in Form No. 9A and Form No.10 in respect of AY 2016-17 where such Form No. 9A and Form No.10 are filed after the expiry of the time allowed under the relevant provisions of the Act.

6. The Commissioners will, while entertaining such belated applications in Form No. 9A and Form No.10, satisfy themselves that the assessee was prevented by reasonable cause from filing of applications in Form No. 9A and Form No.10 within the stipulated time. Further, in respect of Form No. 10 the Commissioners shall also satisfy themselves that the amount accumulated or set apart has been invested or deposited in any one or more of the forms or modes specified in subsection (5) of section 11 of the Act.

(Vinay Sheel Gautam)
Under Secretary to the Government of India

II. GOVERNANCE

1. HOW TO SEND A NOTICE FOR BOARD MEETINGS
2. PREPARATION OF AGENDA
3. WRITING MINUTES

HOW TO SEND A NOTICE FOR BOARD MEETINGS

1. WHAT IS A NOTICE?

1.1 Notice is a communication to the members about the upcoming meeting of the board.

- It is a legal document and has to be legally served.
- The time lines for serving notice for the meeting is part of the incorporation law or the bye laws of the organization

2. WHEN THE NOTICE SHOULD BE SERVED?

2.1 The notice needs to be served in the manner in which it is specified in the law. Generally, there are two types of Meetings for which notice is served i.e.

1. General Body Meeting
2. Governing body/Board Meeting

1. **General Body Meeting:** An Annual General Meeting (AGM) is held once in a year. As per Companies Registration Act 2013, a 21 days' notice is served for calling Annual General Meeting.
2. **Governing Body/Board Meeting:** A Governing body/Board meeting is held at least twice a year, for which a 7 days' notice is to be served.

Further, the notice should be served to every member of the meeting at the address available with the organization.

3. WHO IS RESPONSIBLE TO SERVE THE NOTICE?

3.1 Generally, as per the relevant practices, the Secretary of the Board/General body is responsible to send out the notice in consultation with the Chairperson. Incase, there is no Secretary then the Board or General body can authorize one member to act as a Secretary to serve the notice.

4. HOW THE NOTICE IS TO BE SERVED?

4.1 In the earlier days, the notices were being served as hard copies through registered post or with Certificate of posting. This would provide evidence that the notice was actually served. However, in recent times with the e-mail being the mode of communication, the question arises whether it is necessary to follow the usual route of serving notice through hard copy. Here the incorporation law and the bye laws of the organization come into consideration. For example, if the Societies Registration Act of the state of incorporation provides physical serving of notice, then it has to be followed. Similarly, if the bye laws prescribe serving of the notice through hard copy, it has to be followed accordingly. Otherwise, notice can be served through electronic media (e-mail).

5. WHAT THE NOTICE SHOULD CONTAIN?

5.1 The following should be part of the notice:

a) Name of the organization

b) Date, place and time of the meeting

c) It should be mentioned whether it is an "ordinary meeting" or "Extra ordinary meeting" .

d) The agenda to be discussed should be attached with the notice.

e) The notice should be served by the person authorized (Secretary/Managing Trustee etc)

6. SAMPLE NOTICE

6.1 A sample notice is attached as ***Annexure 1.***

Annexure 1

NOTICE FOR A BOARD MEETING

Notice is hereby given that the 23rd ***(No. of meeting)*** ordinary meeting of the Governing body members of (***"Name of the organization.")*** will be held on (***Date of meeting)*** 20 (***Year)***, at (***Time)*** a.m./p.m. in the registered office at (***Place of meeting)*** to transact the following items/business:

1. Agenda 1
2. Agenda 2
3. Agenda 3

Signature & Seal of Secretary

fmsf

PREPARATION OF AGENDA

1. WHAT IS AN AGENDA?

1.1 Agenda is a schedule of items to be discussed/ decided in a board meeting. An agenda helps in planning the meeting more efficiently, take the right decisions and stick to time.

2. PRE-PLANNING THE AGENDA

2.1 The agenda has to be pre-planned with the key decisions to be taken, the relevant papers to be distributed and any other background material to be circulated beforehand.

3. WHO MAKES THE AGENDA

3.1 The Secretary of the Board is responsible for making the agenda in consultation with the Chairperson.

4. KEY AREAS TO BE COVERED:

4.1 The agenda should include broadly the following sections:

- Welcome & adoption of the agenda
- Review of previous meeting & decisions
- Programme
- Financial
- Organizational
- Any other matter

5. CAN MEMBERS SUGGEST NEW AGENDA ITEM?

5.1 As agenda should be circulated to the members along with the notice (7 to 14 days prior to the meeting). During this time period, the members could suggest or notify new agenda items to be taken up during the meeting.

Incase the member comes up with a new agenda item during the meeting, in that case the Chairperson could allow or disallow the agenda item for deliberation in a meeting. In some cases the agenda item can also be carried forward to the next meeting.

6. CERTAIN OTHER ISSUES TO BE KEPT IN MIND:

6.1 Distributing the approximate time to be allotted to each agenda item

6.2 The key person responsible for initiating or leading the discussion

6.3 Any relevant papers to be attached as agenda notes

6.4 Synchronizing the numbering of the agenda to the probable resolutions that may be taken as an outcome of the agenda item.

7. WHAT SHOULD NOT BE ON THE AGENDA

7.1 Day to day management issues are generally outside the purview of the meeting. It is left to the Chairperson to allow or not allow an agenda item to be included for deliberation in a meeting.

Having a decision-making matrix makes it clear in terms of which decisions are required to be made.

8. SAMPLE AGENDA

Annexure -1

S. no	Table of contents	Time	Discussion led by	Agenda notes	Outcomes
1.	**Welcome & Adoption of agenda**	**9:00-9:45**			
	1.1. Welcome	9:00-9:30	Chairperson		The members are given welcome
	1.2 Adoption of agenda	9:30 -9:45	Chairperson		Agenda is adopted
2.	**Review of previous meeting & decisions**	**9:45-10:15**			
	2.1 Confirmation of minutes of the previous meeting	9:45-9:50	Secretary/ Chairperson	Minutes of previous meeting	Minutes are confirmed
	2.2 Matters arising from the minutes	9:50-10:15	Secretary/ Director	Action taken report	Implementation of previous decisions are reviewed
3.	**Programme**	**10:15-12:00**			
	3.1 Update on programme	10:15-11:15	Program Head/ Staff team	Activity report	Activity report approved
	3.2 Strategic issues if any	11:15- 12:00	Director/Program Head / Secretary	Note on strategic issues	Decision/Resolution to be taken
4.	**Financial**	**12:00-1:00**			
	4.1 Adoption of audited financial statement for the year……….	12:00-12:30	Treasurer/ Finance Head	Audited Financial Statements	Financial Statements Adopted
	4.2 Financial report for the quarter (includes budget variance analysis)	12:30-1:00	Finance Head/ Executive Director	Budget variance analysis for 1st Quarter	The board is updated
5.	**Organizational**	**1:00-1:30**			
	5.1 Policies- any policy to be approved		Executive Director	Relevant policy	Policies are approved for implementation & resolutions taken
	5.2 Change of signatory in bank a/c		Executive Director	Draft resolution	Resolution are passed
	5.3 Staff matters				
	5.3.1 Key changes		H R Head	Note on staff issues	Board is updated
	5.3.2 Staff appraisals		H R Head		
6.	**Any other matter**				

WRITING MINUTES

1. WHAT ARE MINUTES?

1.1 Minutes is defined as a written record of the business transacted and the decision made at a meeting. In a narrow sense, minutes are a record of resolutions passed and matters related to them. Institute of Company Secretaries of India (ICSI) has defined minutes as “a formal written record, in physical and electronic form, of the proceedings of a meeting”

Minutes also serve as an evidence of a meeting. It helps in understanding the deliberations and decision taken.

2. CONTENTS OF THE MINUTES:

2.1 Minutes serve as a record of a meeting. It can also be considered as a legal document. Therefore, the contents of the minutes are very important. The minutes generally consist of the following:

- Background to the agenda: the background should include the advantages and disadvantages of the proposal. It should also briefly describe the impact of the probable decision on its micro and macro environment of the organization.
- Key deliberations & discussions: It should capture the major discussion points of the members. However, recording of specific names of members with their individual views are always avoided.
- Decisions taken: in case of decisions, the rationale of arriving at the decision needs to be clearly captured.

A good minute also records the time of commencement and conclusion of the meeting as well as the venue of the meeting.

3. SOME KEY REMINDERS

3.1 Minutes should be written in clear, concise and plain language

3.2 Minutes should be written in third person and past tense.

3.3 However, resolution should be written in present tense.

3.4 Minutes need not be exact transcript of the proceedings

3.5 Any document, report or notes placed in the meeting and referred to in the minutes should be attached as an annexure. This will preclude the approval of certain documents like audited financial statements, annual report etc.

3.6 Incase an earlier resolution is superseded or modified; minutes should contain a reference to the earlier resolution.

4. FINAL POINT OF REFERENCE

4.1 As a practice, the Secretary also acts as a recording Secretary for the meetings. However, the members may choose to appoint a different person as a recording Secretary. The responsibility of ensuring that the minutes are properly recorded finally rests with the Chairperson. Therefore, the Chairperson is provided with discretion to exclude certain matters which in her/his considered opinion are irrelevant, immaterial or inaccurate representation of the meeting.

5. IS CONFIRMATION OF MINUTES NECESSARY?

5.1 There is a practice to confirm the minutes of the meeting in the subsequent meeting. If we analyze the technicalities and relevance of such a practice, it comes across clearly, that it may not be a big necessity. This is due to the fact that there is a gap of three months to a year in between the meetings. Generally, as a good practice the minutes recorded soon after the conclusion of the meeting is circulated as draft minutes to the members and comments are invited. After incorporating the comments, the final minutes are circulated and decisions/resolutions are acted upon. This deems the confirmation of the minutes in the next meeting irrelevant to large extent. However, this practice can be continued and after the confirmation, the Chairperson can physically authenticate the minutes by signing them post which no changes would be possible/allowed.

6. PRESERVATION OF MINUTES

6.1 Generally, preservation of minutes should be given much importance since they are part of good governance practice and can be used as a legal document. The minutes are maintained in a minute book in a chronological manner. Certain good practices for maintenance of minute book are as follows:

6.2 Minutes book can be in form of loose binding or bound register.

6.3 Minutes can be written by handwriting or can also be computer printouts.

6.4 If they are computer printouts, then after confirmation of minutes they need to be pasted in the minutes book. The Chairperson and Recording Secretary have to sign every page in such a way that part of the signature should be on the minute book and other part to be on the printout pasted. In case it is handwritten, then mere signing in every page should be sufficient.

6.5 The minute book has to be carefully preserved and care should be taken to protect them from fire and other natural calamities.

6.6 Minutes being part of the governance process of the organization needs to be preserved till the existence of the organization.

III. FINANCIAL MANAGEMENT

1. DIFFERENCE BETWEEN COMMERCIAL AND FUND ACCOUNTING SYSTEMS
2. NOTIONAL EXPENDITURES IN DEVELOPMENT PROJECTS

DIFFERENCE BETWEEN COMMERCIAL AND FUND ACCOUNTING SYSTEMS

1. INTRODUCTION

1.1 Commercial organisations have accounting systems that measure product, division and company performance by profit and loss. Accounting in NGOs is also required to measure the inflow and outflow of funds. In addition NGOs also have social and legal responsibilities that extend beyond spending their money wisely. Fund accounting systems help in meeting various social and legal responsibilities which normal accounting systems cannot. Some features of fund accounting are as under:

- Tracking and reporting accounting records separately for different funding sources, grants, programmes etc. and being able to allocate expenses across these group of records
- Tracking and reporting across different time periods (frequently not on annual basis), which often may extend to multiple fiscal years
- Keeping funds separately according to donor's restrictions
- Measuring and analysing the success or failure of each programme or fund individually
- Tracking the ratio of overhead to programme expenses
- Producing specialised and specific reports for internal and external purposes

2. PURPOSE OF FINANCIAL STATEMENT IS DIFFERENT FOR NGOS

2.1 In commercial accounting, financial statements are prepared with a specific purpose for each statement. A profit and loss account is prepared to ascertain the profit and loss during the year. If a company shows high profits then it reflects its success and if it shows losses, it reflects failure. The deficit or surplus in the profit and loss account is directly related with the success or failure of a commercial organisation. However, in an NGO the excess or deficit in an income and expenditure account may not provide any meaningful indication of its success or failure. Suppose an NGO is showing very high income over expenditure, but such high surplus may reflect the inability to spend fund for charitable purposes.

Therefore, something, which is termed as a success in the commercial world, may be treated as a failure in the NGO world.

2.2 Similarly, in the commercial world if the profit and loss account is showing losses it would surely be considered as a failure or negative sign. However, if an NGO is showing excess of expenditure over income it may be a positive sign. The NGO might have done some exemplary work where some money from its past reserves were also spent. On the contrary, due to mismanagement or inefficiencies the cost may have escalated resulting in excess of expenditure over income. Therefore, the deficit in the income and expenditure account cannot conclusively indicate anything about the work or activities of the NGO. It is necessary to obtain more precise and meticulous details of the income or expenditure in order to make any meaningful analysis.

2.3 The moot point is the meaninglessness of conventional accounting statements in context of an NGO. The income and expenditure account fails to provide any definite message about the quality and efficacy of the programmes.

2.4 Similarly, a balance sheet is prepared to signify the state of assets and liabilities at the end of the year. In the balance sheet of a commercial organisation the reader can find

The quantum of external borrowings
- The ratio of equity to loans
- The unsecured and secured loans
- The creditors
- The debtors
- The currents assets, etc.

2.5 Each one of the above can provide a definite insight about the health of a commercial organisation. However, again in the case of an NGO it makes very little sense if we try to understand the health of the programme or project through a conventional balance sheet. We will not be able to know

- the closing balances of individual projects
- negative project balances, if any
- investments pertaining to specific funds
- project-wise assets details
- break-up of capital/endowment funds
- break-up of current restricted funds
- break-up of current unrestricted funds, etc.

2.6 The fundamental difference between an NGO and a commercial organisation is the differential approach towards finance and activities. A commercial organisation does activities to maximise its capital or profits. Therefore, all the energies of a commercial organisation are spent in maximising the profits. On the contrary, NGOs by their inherent constitution do not have any profit motive. All their energies are channelized in maximising the quality of the programme or activities irrespective of whether they are making profits or losses. The donors or the stakeholders will not appreciate if the NGO is amassing huge wealth or is making huge surpluses from its programme. The reader of the financial statements of an NGO is interested in understanding

- the level of competence and efficiency in management of financial resources
- whether the conditions attached to the grants have been complied with or not
- whether different funds coming from different sources have been properly invested and managed according to the conditions attached by the donors
- whether all endowments created are intact and are as per the norms laid down
- whether administrative expenditures are reasonable in comparison to programme expenses, etc.

2.7 The conventional accounting statements may not provide any meaningful insight into the above discussed issues. Therefore, it becomes necessary to maintain sub-system and specific details to generate the desired informations. Fund accounting is one such tool which helps in providing answers to many NGO specific queries. For instance, NGOs create endowments and corpus which may be from internal or external sources. If an endowment fund is created, then it implies that certain amount of funds are blocked permanently or on long term basis for certain specific purpose of activities. Now, it becomes important that the NGO as well as the external stakeholders know about the management and methodology involved in such fund. Therefore, the NGO has to maintain separate details for investment, assets, cash and bank balances on account of this particular fund. Similarly, the NGO also has to separately maintain the detail of expenditures made on account of this fund. Fund accounting becomes necessary for maintaining specific fund or activity-wise detail.

NOTIONAL EXPENDITURES IN DEVELOPMENT PROJECTS

1. UNDERSTANDING NOTIONAL EXPENDITURE

1.1 In this chapter, we shall be discussing the concept and prevailing practices of Notional expenditures in development projects.

1.2 Notional income or expenditure generally denotes something, which remains unutilized or accrued at the project or fund level, but there is no real expenditure or income at the level of the organisation. For example, if an organisation charges rent in a particular project for the use of its own premises, such rent will result in a notional expenditure in that particular project and at the same time will result in a notional income in the general fund/account of the organisation.Similarly, notional expenditure can be created by various methods including charge of expenditure on approximate basis or even inflating the expenses.

1.3 Notional expenditure generally is also valued at the estimated difference between the market value of the goods or services provided and the actual cost incurred by the party.

1.4 It has been seen that some donors permit notional expenditure as a basis for recovering administrative expenses. For instance, a project budget may be allowed 10% of the project cost as administrative charge. In such circumstance, the organisation will collect 10% of the project cost as administrative expenses but the actual administrative expenditures may be higher or lower than the amount charged.

1.5 In normal accounting parlance, certain legitimate non-cash expenditures are also referred to as notional expenditures. Depreciation is an example of such non-cash notional expenditure. In case of depreciation the term notional may not be entirely relevant because it actually denotes the wear and tear or the loss in the value of the asset. However, in development projects, normally non-cash expenditures are not considered as a part of the budget as the project assets are also financed under the project cost. Therefore, the possibility of charging further depreciation in the same project does not arise.

2. DIFFERENCE BETWEEN COMMERCIAL CONTRACT & NPO PROJECT CONTRACT

2.1 In a commercial contract, generally a client is billed against invoices at a predetermined rate of goods and services. For example, a commercial organisation may charge @5000/- per person per day but the actual expenditure may be much less than Rs 5000/- per day. In such cases, the commercial organisation will book actual expenditures against such receipts and the profit and loss shall be automatically determined at the end of the year. However, in the case of an NPO, expenditures are charged at an estimated rate of, say, Rs 5000/- which may be much less than the actual payment, then it will result in notional expenditure as well as notional income. This is because the utilisation statement has been prepared on the basis of the estimated rate and not the actual expenses and being the non-profit organisation, profit cannot be booked.

It may also be noted that, all NPO projects are subject to actual utilisation of funds. Therefore, in a project contract estimated or notional expenditure should not be booked as actual utilisation of funds. If estimated or notional expenditures are booked as actual expenditures, then, funds are not actually applied to that extent and would tantamount to diversion of project funds.

3. WHY LEGALLY NOTIONAL EXPENDITURE IS NOT PERMISSIBLE

3.1 To incur a valid expenditure it is necessary that there is a valid transactions between two parties. All expenditures to be legally valid would require a valid legal transfer of funds against a valid invoices for goods or services. It is a established legal dictum that ***one cannot trade or transact with oneself***. Therefore, whenever there is a transfer of funds from one project to the general fund or another project, the fact remains that there is no legal transaction as far as the organisation as a whole is concern. The inter project transactions get nullified at the time of consolidation.

For Example : An NPO charges Rs 200/- per head towards the food provided to the participants in a Seminar conducted at its own building. The NPO transfers ' 10,000/- to its general funds from the project account as expenditure against fooding of participants. However, in its general account the actual expenditure against fooding is 4,000 only. Therefore, there is a profit of Rs 6,000/- in a general account. In this case in the project account Rs 6,000/- was charged over & above the actual expenditure. Therefore, there is a profit of six thousand in the general account. In other words, the NPO as a legal entity does not gain or loose anything, but, there is a loss of Rs 6,000/- in one project and gain of Rs 6,000/- in the general account i.e. transferring funds from one pocket to another. Further for greater clarity the following are characteristic of such transaction:

- The service provider and the recipient are the same person.
- No legal transaction or transfer with oneself
- There is a notional charge of expenditure in one project to the extent of Rs 6,000/-.
- There is a matching notional profit in general account to the extent of Rs 6,000/-
- For donor utilisation purposes the utilisation statements shall be inflated to the extent of Rs 6,000/-, however the consolidated accounts will show the correct expenditure as only actual expenditure is permissible under the income tax and FC laws. Therefore, the '6,000/- will be just transferred from the project account to the general account without any legal implications.

4. COMMON PRACTICES OF NOTIONAL EXPENDITURE

4.1 Some of the common practices of notional expenditures in the NPO sector are as under:

- Charge against use of building
- Charge against use of infrastructure, convention centre etc.
- Charge against use of vehicle
- Charge against use of photocopier, telephone, computer etc.
- Providing services at a pre-determined rate
- Charge of salary of the same staff to various projects.
- Inequitable apportionment of common expenditure etc.

4.2 In the following paras some case studies and methodology of various common practices of notional expenditure have been discussed.

5. GOODS AND SERVICES PROVIDED AT A FIXED RATE

5.1 There are instances where the organisation provides goods and services at pre determined prices. For instance, the organisation may charge for food against number of participants in meetings and training at a fixed pre-determined rate whereas the actual expenditure may be much lower.

Similar to the example discussed earlier, XX NPO conducts training and conference for the beneficiaries throughout the year. Its trainings are generally residential inclusive of food and accommodation. All participants stay in the building owned by XX. XX charges ‘ 200/- per day per participant towards food and ‘ 300/- towards accommodation. The money charged to the project is transferred to the general account. The actual expenditure on food and maintenance of property is incurred from the general account. It was found that the actual expenditure was ‘ 100/- per day per participant towards food and ‘100/- towards accommodation. In this case, XX has charged notional expenditure of ‘100/- per day per participant towards food and ‘200/-towards accommodation.

The above example shows charging of notional expenditure which is not an acceptable practice in a project contract. The expenditure is not actual to the extent transferred to the General Fund. A partner organisation is not allowed/supposed to make profit from development projects. From a legal perspective also such expenditure are not permissible, because the law would allow only the actual expenditures as one cannot trade with itself. In such cases one project of the partner is the service provider and another project is the service recepient which is legally not permissible.

6. RENT AND SERVICE CHARGE AGAINST ASSETS

6.1 There might be instances where the organisation charges the project against use of its assets. The assets could be land and building, training and conference facilities, vehicles, telephone, photocopier etc. In this context it is important to note that there might be some legitimate expenditure even without a legal transfer. For example, a LCD Projector is used for trainings and the effective life of the projector is 4 years. If the projector is used for, say, 500 trainings, then the actual cost should be distributed over the 500 trainings. The difficulty arises because donors do not, normally, allow depreciation against common assets as a part of the project cost. In such cases any such transfer against such facilities may not necessarily be a notional expenditure, but estimation of such expenditure should be made with prior approval of the donor. The following points needs to be kept in mind:

– If the charge is against use of the building, it should be seen whether the building is owned or rented. In case the building is owned by the organisation it should be clarified whether the building has been created out of corpus funds or accumulated reserves or any other sources. The building or properties even though owned by the NPO may have been created out of project funds also. Therefore, one may be subjected to three types of circumstances where rent or charges are collected against building or properties:

  (i) Building or properties created out of corpus funds or accumulated reserves

  (ii) Building or properties created out of the project funds or from past projects of the same donor.

  (iii) Building or properties created out of funds provided by other donors.

– **Rent in case of self owned property created out of corpus funds or accumulated reserves** : Any recovery made against such assets should be transparently disclosed at the project proposal stages and should be formally reflected in the project agreement. Further, the rent/ charges recovered should be comparable with the reasonable market rent. In such cases it is necessary to assess the purposes for which the building is used i.e. for programme or administrative purposes. Further, normally, it is expected that the NPO should also contribute to the budget work, therefore the clarity and rationale for such transaction needs to be established between the donor and the NPO.

– **Rent in case of self owned property created out of the project funds or from past projects of the same donor** : No recovery should be made against use of such assets for project purposes. The implementing partner should declare that no notional expenditure have been charged against the assets funded by the same donor.

– **Rent in case of self-owned property created out of funds provided by other donors:** Normally no recovery should be made against use of such assets for project purposes. However, if there is a circumstantial justification for use of such assets then the rent or cost charged against such assets should be transparently disclosed at the project proposal stages and should be formally reflected in the project agreement. Further, the rent/charges recovered should be comparable with the reasonable market rent.

– **Rent against other infrastructure and assets such as training facilities, equipments etc.:** When an organisation recovers the cost of the assets owned by it, then it becomes important that such cost recovery mechanism is transparently disclosed at the project proposal stages and is formally reflected in the project agreement. Any internal recovery/ gain by the organisation is not permissible unless it is formally approved by the donor. The same rationale of the source of such assets is also applicable i.e. whether such assets are corpus assets or project assets needs to be seen and the treatment should be as discussed above with regard to self owned property.

– **Multiple Rent in case of a rented building:** It should be ensured that the sum total of the rent charged to various projects does not exceed the total actual rent paid. If the rent charged to various projects exceed the actual rent then it will result in notional expenditure as well as income for the organisation.

– **Rent in case of self owned car/vehicle, photocopier and other assets:** The same principle should be applied as have been illustrated in context of self owned building or properties. Further the rent charged should be comparable with the reasonable market rent and the permission from the donor in this regard should also be obtained at the proposal stages.

– **Rent and other charges paid to sister concerns of the organisation:** Such conflict of interest transactions should be done with prior approval of the donor and should be declared and disclosed. Such transactions may also be in violation of the provisions of the local laws such as the Income Tax Act in India.

7. ADMINISTRATIVE EXPENDITURE AS A FIXED CHARGE

7.1 There might be instances where the organisation charges the administrative expenses as a fixed charge i.e the organisation may charge 20% of the project cost as administrative expenditure. In such circumstances the project agreement needs to be adhered to for the approval of the donor in this regard. Any other administrative expenditure which are charged to the project over and above the fixed administrative charge are not admissible.

7.2 Some donor might permit such charges for some small or specific projects. However, legally such charges do not constitute valid expenditure therefore, it is not permissible to treat such expenditure as valid utilisation of project funds.

8. INFLATING SALARIES TO CREATE BOTH NOTIONAL INCOME & EXPENDITURE

8.1 There might be instances where the organisation charges inflated programme expenditures and subsequently the additional amount charged to the project is transferred to the general fund by creating notional income. The case study in the box below will clarify the issue further.

ZZ NPO is distributing funds among beneficiaries for purchase of seeds and manure. It pays '10,000/- per beneficiary for 100 persons. However, on the same day of the payment to the beneficiaries, all the beneficiaries make donation of '5,000 back to the organisation. In this way ZZ is able to transfer 0.5 million rupees to its general funds by charging notional expenditure in the project and by showing notional income in the general account.

9. CHARGING COMMON EXPENDITURE TO VARIOUS PROJECTS

9.1 There might be instances where the organisation charges common expenditure to various other projects. The common expenditure may be rent of premises, brochures and materials for similar programme etc. It may be noted if the common expenditure has been already funded by one particular donor, the same expenditure should not be charged again to various other projects and donors.

9.2 In case the common expenditure is shared by various donors, it needs to be ensured that the sum total of the expenditures charged to various projects is not more than the actual expenditure incurred by the organisation. In various instances it has been found that the same programme or activity has been shown as expenditure to more than one projects. In such circumstances it is important to ensure that if two projects of similar activities are implemented then there should be adequate disclosure and internal control with regard to double booking of expenditures.

10. CREATING PROVISION FOR EXPENDITURE & SUBSEQUENTLY TRANSFERRING IT TO GENERAL FUND

10.1 There might be instances where the organisation creates provision for expenditure and charges it to the project. In other words, the reporting to the donor reflects a notional expenditure which is just the provision and has not been actually incurred. In the subsequent year the same provision may be transferred as surplus to the general fund. Wherever non cash expenditure is incurred or expenditure is charged based on accrual basis of accounting (i.e. where the cash is still with the organisation but utilisation is shown to the donor), it needs to be ensured that the amount so provided is actually paid in the subsequent year.

11. CHARGING NOTIONAL CONVEYANCE AND ALLOWANCES AGAINST STAFF

11.1 There might be instances where the organisation charges notional amount as conveyance, allowances and reimbursements to staff. In other words, there is no actual expenditure but a considerable amount is charged to the project against various staff as daily conveyance, refreshment allowance and other permissible unsubstantiated expenditures. It needs to be ensured that there are no notional expenditures and matching notional income in this regard.

IV. CSR

1. FOREIGN & INDIAN COMPANIES SUBJECT TO FCRA UNDER CSR
2. TAX IMPACT UNDER VARIOUS TYPES OF CSR ACTIVITIES

FOREIGN & INDIAN COMPANIES SUBJECT TO FCRA UNDER CSR

1. SUMMARY OF THE CHAPTER

1.1 The CSR law applies to Indian as well a foreign companies working in India. CSR involves charitable activity and grant making. In India, giving grant to other NPOs, is subject to the Foreign Contribution Regulation Act (FCRA), 2010. Therefore, it is important to understand the applicability of FCRA on CSR activities.

1.2 Under FCRA, foreign companies and even Indian companies are not allowed to provide grant to other NPOs, unless they have FCRA prior permission for registration. There are many Indian companies having more than 50% share holding by foreigners. Such companies should be careful while providing CSR grants to other NPOs.

1.3 In fact, all funds provided without consideration by such companies are treated as foreign contribution. Therefore, such companies cannot even setup an Indian Trust or Society by making initial contribution/ expenditure, because technically, even for such initial contribution/ expenditure, permission from FCRA department is necessary.

1.3 Such companies are treated as 'Foreign Source' and for the technical purposes of FCRA, such companies cannot do any charitable activity in India without prior permission. In this chapter, the FCRA law pertaining the foreign source has been discussed.

1.4 Indian companies like ICICI Bank Ltd., HDFC Bank Ltd., Maruti Suzuki India Ltd. etc. cannot give CSR grants to other NPOs, if such NPOs (including their own foundations) do not possess FCRA prior permission or registration.

2. MEANING OF 'FOREIGN SOURCE' UNDER FCRA

2.1 The term 'foreign source' has not been specifically defined under the FCRA. Unlike the term 'foreign contribution' which has been defined specifically, the term 'foreign source' has been only given an inclusive definition in FCRA. The statutory definition of 'foreign source' as per Section 2(1)(j) of FCRA, 2010 is as follows :

– "foreign source" includes, —

– the Government of any foreign country or territory and any agency of such Government;

– any international agency, not being the United Nations or any of its specialised agencies, the World Bank, International Monetary Fund or such other agency as the Central Government may, by notification, specify in this behalf;

– a Foreign company;

– a corporation, not being a Foreign company, incorporated in a foreign country or territory;

– a multi-national corporation referred to in sub-clause (iv) of clause (g);

– a company within the meaning of the Companies Act, 1956, and more than one-half of the nominal value of its share capital is held, either singly or in the aggregate, by one or more of the following, namely:—

A. the Government of a foreign country or territory;

B. the citizens of a foreign country or territory;

C. corporations incorporated in a foreign country or territory;

D. trusts, societies or other associations of individuals (whether incorporated or not), formed or registered in a foreign country or territory;

E. Foreign company;

– a trade union in any foreign country or territory, whether or not registered in such foreign country or territory;

– a foreign Trust or a foreign foundation, by whatever name called, or such Trust or foundation mainly financed by a foreign country or territory;

– a society, club or other association of individuals formed or registered outside India;

– a citizen of a foreign country."

2.2 As it is evident, the term "foreign source" has not been defined exhaustively. The Act has given an inclusive definition of the term 'foreign source' and that includes the sources mentioned in clauses (i) to (x).

2.3 Important: It may be noted that under clause (vi) above, a foreign source includes an Indian company if more than 50% of its share capital is held by persons covered under foreign source. Therefore, care should be taken before receiving local donations and grants from Indian companies and it should be ensured that more than 50% of the share capital is held by Indian promoters, otherwise it will be treated as foreign contribution.

3. WHAT IS A FOREIGN COMPANY UNDER FCRA

3.1 The statutory definition as per Section 2(1)(g) of FCRA 2010 of 'foreign company' is as follows :

"(*g*) "Foreign company" means any company or association or body of individuals incorporated outside India and includes—

– Foreign company within the meaning of Section 591 of the Companies Act, 1956;

– company which is a subsidiary of a Foreign company;

– the registered off ice or principal place of business of a Foreign company referred to in sub-clause (i) or company referred to in subclause(ii);

– a multi-national corporation.

Explanation.—For the purposes of this sub-clause, a corporation incorporated in a foreign country or territory shall be deemed to be a multi-national corporation if such corporation,—

– has a subsidiary or a branch or a place of business in two or more countries or territories; or

– carries on business, or otherwise operates, in two or more countries or territories."

To determine whether a company is a foreign company or not, the provisions of Section 591 of the Companies Act, 1956 are relevant. Basically, the provisions consider any company as foreign company, if it has been incorporated outside India and has a place of business within India. Provisions of Section 591 are reproduced as under:

“591. Application of sections 592 to 602 to foreign companies.—(1) Sections 592 to “4. Meaning of ‘holding company’ and ‘subsidiary’ - (1) For the purposes of his Act, a company shall, subject to the provisions of sub-Section (3), be deemed to be a subsidiary of another if, but only if,—602, both inclusive, shall apply to all foreign companies, that is to say, companies falling under the following two classes, namely:—

i. companies incorporated outside India which, after the commencement of this Act, establish a place of business within India; and

ii. companies incorporated outside India which have, before the commencement of this Act, established a place of business within India and continue to have an established place of business within India at the commencement of this Act.

Notwithstanding anything contained in sub-Section (1), where not less than fifty per cent, of the paid-up share capital (whether equity or preference or partly equity and partly preference) of a company incorporated outside India and having an established place of business in India, is held by one or more citizens of India or by one or more bodies Corporate incorporated in India, or by one or more citizens of India and one or more bodies Corporate incorporated in India, whether singly or in the aggregate, such company shall comply with such of the provisions of this Act as may be prescribed with regard to the business carried on by it in India, as if it were a company incorporated in India.”

Subsidiaries are also included : The subsidiary of a foreign company, even if it is an Indian company is also considered as foreign source under FCRA. Again, to determine whether a company is a subsidiary of a foreign company or not, the provisions of Section 4 of Companies Act, 1956 are relevant which are reproduced as under

“4. Meaning of ‘holding company’ and ‘subsidiary’ - (1) For the purposes of his Act, a company shall, subject to the provisions of sub-Section (3), be deemed to be a subsidiary of another if, but only if,—

– that other controls the composition of its Board of Directors; or

– that other—

    i. where the first-mentioned company is an existing company in respect of which the holders of preference shares issued before the commencement of this Act have the same voting rights in all respects as the holders of equity shares, exercises or controls more than half of the total voting power of such company;

    ii. where the first-mentioned company is any other company, holds more than half in nominal value of its equity share capital; or

– the first-mentioned company is a subsidiary of any company which is that other’s subsidiary.

  Illustration : company B is a subsidiary of company A, and company C is a subsidiary of company B. company C is a subsidiary of company A, by virtue of clause (c) above. If company D is a subsidiary of company C, company D will be a subsidiary of company B and consequently also of company A, by virtue of clause (c) above, and so on.”

Important : It may be noted that FCRA makes a reference to the definition of foreign company and subsidiary company as it existed in the Companies Act, 1956. There is no reference of Companies Act, 2013. However, for the purposes of CSR grant, the difference between two definition is not relevant under FCRA.

4. THE CHANGES IN DEFINITION OF ‘FOREIGN COMPANY’ AFTER COMPANIES ACT 2013

4.1 The FCRA 2010 make a reference to the Companies Act, 1956 as it was enacted prior to the enactment of the Companies Act, 2013. The definition of foreign company in the Companies Act, 2013 is as under:

“Section 2 (42)

“Foreign company” means any company or body Corporate incorporated outside India which –

– has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

– Conducts any business activity in India in any other manner.

Further, Section 379 under Chapter XXII requires a company to register under the companies Act, 2013 and for other compliances in India :

Section 379 – Companies incorporated outside India

Where not less than fifty per cent of the paid-up capital, whether equity or preference or partly equity and partly preference, of a Foreign company is held by one or more citizen of India or by one or more companies or bodies Corporate incorporated in India, or by one or more citizens of India and one or more companies or bodies Corporate incorporated in India, whether singly or in the aggregate, such company shall comply with the provisions of this Chapter and such other provisions of this Act as may be prescribed with regard to the business carried on by it in India as if it were a company incorporated in India.

Section 379 has become effective from 12th Sept. 2013.

TAX IMPACT UNDER VARIOUS TYPES OF CSR ACTIVITIES

1. INTRODUCTION

1.1 The corporates would be more inclined to make CSR donations in schemes with tax incentives such as 80G, Section 35, Section 35AC etc., because of the tax benef its. If the corporate does direct CSR spending then the effective tax rate will increase. For instance, the corporate tax rate is currently 33.9% inclusive of surcharge, if the company undertakes direct CSR activities then to spend 2% on CSR the company will have to pay another approximately 1% as taxes as CSR expenditure can be done from post tax income.

1.2 On the other hand, if a corporate undertakes CSR activities thr0ugh Section 80G registered NGOs, then it will get 50% tax advantage, and will still have to pay another 0.5% approximately as tax, since CSR expenditure can be done from post tax income after 50% tax rebate.

1.3 Further, if a corporate undertakes CSR activities thr0ugh NGOs registered under Sections 35 & 35AC or through funds like Prime Minister Relief Fund, National Defence Fund having 100% tax benef it under Section 80G, then it will get 100% tax advantage and will not be required to pay any additional taxes on account of CSR.

2. CONCLUDING REMARKS

2.1 Overall the recent changes in Income Tax Laws have created a fix with regard to the admissibility of the CSR expenditures. It is the job of the government to align various legislations. The Companies Act, 2013 mandates various types of CSR expenditures including giving grant to Prime Minister Relief Fund, National Defence Fund, etc. The Act also provides a list of priority activities under Schedule VII, which the companies can undertake under CSR. Now slum development will also be included as CSR expenditure.

2.2 However, differential tax treatment of the legally permissible CSR expenditure will defeat the very purpose of enacting various priority activities under CSR. Why should a company incur CSR expenditure on priority areas without having any tax benef it, when it can incur the same with 100% tax deductions ? The Government should provide a level playing ground for all kinds of CSR expenditure.

2.3 It is proposed to clarify that for the purposes of Section 37(1) any expenditure incurred by an assesse on the activities relating to corporate social responsibility referred to in Section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and hence shall not be allowed as deduction under Section 37. However, the CSR expenditure which is of the nature described in Section 30 to Section 36 of the Act shall be allowed deduction under those sections subject to fulfilment of conditions, if any, specified therein.

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