



# KPB & Associates

## Taxing donations made by one charitable or religious institution to another

### Background

In the world of philanthropy, well-known charitable or religious institutions often receive the most donations. This is because they have a wider reach and are more recognized in philanthropic circles. However, this means that lesser-known charitable or religious institutions may receive fewer donations, even if they are doing important work at the grassroots level. To address this disparity, well-funded trusts often donate to smaller trusts.

This alert explores the tax implications of donations made by one charitable or religious institution to another in India. It outlines how recent amendment under the Income Tax Act of 1961 (the Act) may cause undue hardship on the grant of donations by one charitable or religious institution to another.

### Restriction on donations made by one trust to another out of the income of the current year

Upto 31<sup>st</sup> March 2023, 100% of the amount of any donation made by one trust to another out of the income of the current year was considered to be an application of income for the donor trust. However, effective from 1<sup>st</sup> April 2023 this has now been reduced to 85%.

This amendment applies to both charitable organizations and organizations established for religious purposes, irrespectively whether the recipient charitable or religious institutions applies the donation towards its activities carried on by itself or through anyone else.

To illustrate, the Established Foundation (donor) has granted a donation of Rs. 2,00,000/- to the New Foundation(donee)

Particulars	Upto 31-3-2023	Post 1-4-2023
<b>Income from property held under the Trust</b>	Rs. 10,00,000	Rs. 10,00,000
<b>Donation to other Trusts</b>	Rs. 2,00,000	Rs. 2,00,000
<b>Less: Donation to other Trusts allowable as a deduction</b>	Rs. 2,00,000	Rs. 1,70,000 (85% of Rs. 2,00,000)
<b>Less: Other Charitable &amp; Admin Expenses</b>	Rs. 6,50,000	Rs. 6,50,000
<b>Less: Exemption of 15% u/s. 11(1)(a)</b>	Rs. 1,50,000	Rs. 1,50,000
<b>Income subject to tax after exemption</b>	Rs. NIL	Rs. 30,000

Thus, post amendment, Established Foundation will be subjected to tax @ 30% on the entire amount of Rs. 30,000/- u/s. 115BBI of the Act without the basic exemption limit.

#### Revenue Justification

It is stated that the reason for this amendment is to prevent trusts from avoiding paying tax by simply donating their income to other trusts. Any Charitable or religious institution is required to apply at least 85% of its total income. On application of 85% of its income, the balance of 15% is tax-exempt and allowed to be accumulated without any restrictions.

The legislative intent of the amendment is to deter trusts from circumventing the 85%

application of income requirement by forming multiple trusts and accumulating the 15% at each layer. This practice, known as "cascading trusts," allows trusts to reduce the amount of income that is actually applied to charitable or religious activities. By forming multiple trusts, each of which applies only 85% of its income, the effective application of income can be reduced to a much lower percentage.

#### Implications

The amendment aims to prevent this practice by limiting the amount of donation that can be considered as application of income to 85%. However, amendment leads to creating undue harassment to the donor trust.

Firstly, where the donor trust intends to avoid payment of tax, it will have to spend, an additional sum equivalent to 15% of the donation so made to the donee trust, towards the activities of the donor trust.

Where the above option is not viable, the donor trust will have to pay tax.

However, where the donor trust, being a charitable or religious institution, has spent the whole of their income received during the year, it is left with no funds, either to pay the tax or to spend the additional amount of 15% which is not being allowed as a deduction.

Thus, the new provisions inadvertently impede the operations of smaller charitable or religious institutions that are making a significant impact at the grassroots level.



## Key Contacts – Direct Tax

At K P B & Associates, we are a Chartered Accountancy firm committed to elevating your business performance through knowledge-driven solutions. Our overarching vision is to establish ourselves as a paragon of excellence and efficiency, dedicated to furnishing bespoke professional services for our valued clientele. With a legacy spanning over two decades, we bring forth a wealth of experience to offer superior solutions in assurance, risk management, internal audit, regulatory compliance, financial advisory, and business consultancy.

Navigating today's rapidly evolving business landscape requires adaptability. In the midst of this dynamic and demanding milieu, we provide a beacon of clarity, underpinned by a tradition of client-centric service, a trajectory toward excellence, and an unwavering commitment to ethical standards in every project we undertake.

KPB is founded upon a bedrock of fundamental principles:

- **Professional Expertise:** We house a team of accomplished multidisciplinary professionals and capable assistants, continuously honing their skills with up-to-date technical knowledge to meet our clients' diverse needs.
- **Ethical Business Practices:** Our operations are rooted in unwavering ethical standards, ensuring integrity in all our dealings.
- **Responsiveness to Client Needs:** Our approach is highly responsive to the unique requirements of each client, fostering effective collaboration and tailored solutions.
- **Value for Money:** We offer optimal value for our clients' investments, ensuring that the services provided align with their objectives.

Our partners actively contribute to knowledge dissemination by crafting articles for diverse professional publications, newspapers, magazines, and more. Furthermore, they assume roles as educators, imparting their expertise at seminars, conferences, and within various organizations, covering a broad spectrum of technical subjects.

What sets us apart is our comprehensive suite of integrated services, encompassing Taxation, Audit and Assurance, Risk Management, Forensic Analysis, Insolvency Resolution, Business Administration, Financial Consultancy, Regulatory Advisory, Valuations, and more. We stand ready to be your steadfast ally in propelling your business toward excellence and prosperity.

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**Priti Savla**  
Partner  
[priti@kpbca.com](mailto:priti@kpbca.com)

**Paras Savla**  
Partner  
[paras@kpbca.com](mailto:paras@kpbca.com)

**Prity Dharod**  
Partner  
[prity@kpbca.com](mailto:prity@kpbca.com)

**Archana Kshatriya**  
Associate Consultant  
[Archana.Kshatriya@kpbca.com](mailto:Archana.Kshatriya@kpbca.com)

Visit us [www.kpbca.com](http://www.kpbca.com)

### Our Offices

904, Centrum, Opp. Rayladevi Lake,  
Next to IMCOST, S G Barve Road, Thane 400 604  
MH India T: +91.22.2582 7822/38

1004, Level 10, Sunshine Tower,  
Senapati Bapat Marg, Prabhadevi, Mumbai 400 013  
MH India T: +91.22.2432 2258/68