A good tax system has been the quest of all good societies and for good reasons. Taxes have profound impact on the economy and on the perceptions of the people about the fairness of the entire system. Hence the attributes of a good tax structure have been a subject of great interest among experts and laymen alike. Unfortunately, what experts consider as the "ideal" is rarely attainable in the real world. For one thing, no country can start its tax system from scratch while transition to the ideal or even the desired pattern is often fraught with difficulties. Besides given the revenue requirements of the government, any reform, if it is to be acceptable has to be revenue neutral. Then there are the constraints of administrative feasibility especially in countries with a large unorganised sector. Nevertheless, major reforms of tax system have been carried out in many countries even in the developing world to attain simplicity, fairness and efficiency. Thinking of fiscal
economist has been a key input in this endeavour.¹

While proposing the guiding principles underlying the tax reforms, the Tax
Reforms Committee (Commonly known as Chelliah Committee) in its interim Report recommended:

"The tax system and law should be as simple as possible: it
should have the strictly limited objectives of raising revenues
for the Government in a fair and efficient manner, achieving
redistribution and discouraging some industries in the use or
consumption of some products as well as granting a reasonable
degree of protection to domestic industries. A simple system
will have only a limited number of rates and exemptions or
deductions and give the least possible discretionary power to
the tax officials for interpreting the law.

Methods of tax administration should be modernised and tax
enforcement should be visibly improved."

In our country tax reforms relating to charitable trusts have been the subject
matter of investigations on a number of occasions. As a result, changes have also been
made in the tax statutes. However the problem continues to elude a satisfactory solution.
Following certain recommendations made by the Direct Taxes Administration Enquiry
committee in 1958-59, the provisions in the Act relating to charitable trusts were over-
hauled. While this might have improved the position it still left loopholes. The Tax
Evasion Enquiry Committee pointed out in 1968 that "trust" continue to be used as one
of "tax-dodging" devices. They went on to say: "Charitable trusts are created with a corpus
of concealed income masquerading as donations from a large number of ghost  or

¹ Bagchi Amaresh, Introduction and Summary on Symposium on Trends in Tax Reform, National
Institute of Public Finance and Policy (Unpublished)
anonymous donors. Exemption is obtained in regard to the income of these trusts although a suitable portion of the trust funds and income, in fact, remains at the disposal of the donor himself through handpicked assesses. Even businesses are carried on by such trusts created ostensibly for charitable purposes.\textsuperscript{2}

Charitable trusts serves a very laudable objective. At the same time unscrupulous elements have been and continue to employ them as tax dodging devices. This is a phenomenon that is universally prevalent. In the United Kingdom, a Royal Commission which investigated the problem found that a number of trusts managed to avoid tax, though they were conducting activities which "have no real connection with the idea of charity at all". In the United States of America, the Ways and Means Committee of the House of Representatives pointed out in 1969 that "unlimited" deduction on account of charitable contributions "has allowed a small number of high income persons to pay little on tax on their income".\textsuperscript{3}

Income from property (including specified businesses) held for charitable or religious purposes, which are for the benefit of the community or a well defined section of the community, is exempt from tax. However, attempts were made in the past to ensure that business and family trusts are not utilised for splitting income for tax purposes or for retaining controlling interest in the associated concerns, have resulted in making the provisions complicated.

\textsuperscript{2} The Report on action taken by the Government on recommendations made by the Public Accounts Committee in its 121st report in 1970.

\textsuperscript{3} \textit{Ibid.}
The definition of the word "Charitable Purpose" which was at one stage loosely defined, underwent vital change many times, in order to circumvent the decision of Privy Council in the case of *Re Trustees of The Tribune*. The Privy Council held that the income of the trust running a printing press and a newspaper was exempt from tax as the object was, if not education, advancement of an object of general public utility viz., to supply the province with an organ of educated public opinion. This decision opened the flood gates to tax avoidance as every business, being run by a trust for the benefit of general public could be considered to be for the "general public utility".

The definition of ‘Charitable purpose’ was amended and ‘ten’ controversial words not involving the carrying on of any activity for profit were added after the words *object of general public utility* in the Income-tax Act, 1961 so that the last or general category of objects of general public utility is qualified by the need to show that it did not involve any activity for profit. These ten words opened the flood gate of eternal litigation, when the position become more and more blurred the Government on the recommendations of *Chokshi Committee* and on the basis of the Supreme Court decision in *CIT v. Surat Art Silk Cloth Manufacturers Association*, deleted these words from the definition of ‘Charitable purpose’ by the Finance Act, 1983 and inserted section 11(4A). Section 11(4A) underwent a change by the Finance Act, 1991 that the business of a trust must be incidental to the attainment of the objectives of the trust and separate books of account are maintained by such trust in respect of such business.

4 (1939) 7 ITR 415 (PC).
5 (1980) 121 ITR 1 (SC).
The reasons for the amendment are many and weighty. One of them is that it will be inequitable to place a manufacturer or trader in a position of disadvantage by granting a tax concession to a trust producing or dealing in the same commodity in the same market. But if the profits of that business of the trust are incidental to the attainment of the objectives of the charitable trust then such tax immunity is allowed provided separate books of account are maintained by such trust in respect of such business. Therefore, it is submitted that the present definition of 'charitable purpose' and treatment of income from business activity of a charitable trust is free from flaws.

Some judicial decisions ⁶ held that if the primary object of a trust was of a charitable nature and preference would be given to the needs of the relations and family members of the donor, the trust would be eligible for tax exemption. These decisions are tending to generate tax avoidance where the trustees are asked to give preference to the poor relatives of the donor and entire income is spent only on the relatives of the author.

One of the most important requirement of a valid charity is its public character. It must be for the benefit of public at large or a section of it. But the purpose of charity will be lost when "the preference to need of poor relatives" clause is made in the trust deed. Therefore, it is submitted that the present position be changed by an amendment. In such cases where any preference clause is made in the trust deed, it should not be treated as valid charity, to qualify for exemption from tax under section 11 of the Income-tax Act, 1961.

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6 Trustees of Charity Fund v. CIT (1959) 36 ITR 513 (SC); D.C. Anir v. CIT (1945) 13 ITR 465; CIT v. Meghji Mathurdas Charity Trust (1959) 37 ITR 419; CIT v. Deshpande (1976) 102 ITR 390;
As regards the accumulation and application of income of a charitable trust and institutions, the income that is allowed to be accumulated for application to charitable and religious purposes should not exceed 25 percent of the aggregate of the income from trust property, even if the accumulation is in excess of 25 per cent of the income of trust or institution would be entitled to exemption from tax if a written application on prescribed form 7 to that effect is given to the Assessing Officer. This concession given to charitable trusts is sometimes misused by the trusts by withholding the funds from charity. For this it is submitted that if more than 25 per cent of such income of a trust is set apart for being spent subsequently for charitable purposes, the amount set apart in excess of 25 percent should be taxed in the year in which it is so set apart.

The voluntary contributions in kind like jewellary, ornaments, hundies and other valuables offered to religious trusts are sometimes misappropriated by the functionaries of trust. Trust like Tirumala Devasthanam Tripiti temple get offerings in shape of ornaments, hundies etc. Except honesty of the trustees there is no other way to check pilferage of funds of such trusts. It is submitted that where contributions are received by trusts in any form other than cash, handling should be done in the presence of honest functionary of the Government or his nominee.

The legislative amendment of 1989 empowers the charitable trusts and institutions to receive voluntary contribution by way of donations towards the corpus of the trust without making the trust liable to tax or without making such trust or institution spend the moneys in any specified manner or according to the directions of the assessing authorities. It means the voluntary contribution by way of corpus donations can properly be received by the charitable and

7 From No. 10A appended as Annexure 1 with this work.
religious trusts and institutions and exemption can be claimed even if the funds forming part of the corpus had not been applied or accumulated like other income of the trust. Many tax authorities do not agree with the plea of the trust for exemption from tax inspite of many judgements it would be appropriate for the Central Board of Direct Taxes to clarify the above legal position by an elaborate Circular to avoid futile litigation.

Under the law as it is at present, a charitable trust can claim exemption on the investment of corpus funds into any shares and debentures in a company, even though for a long period of time, the trust funds may be invested and utilised for furthering the donor’s business interests, the income of the trust would, nonetheless, continue to enjoy exemption from tax. For example, where an industrialist created a trust for charitable purposes but stipulated that for a period of 18 years the trust funds and the income therefrom was to be invested in the shares of a company through which the donor controlled other companies in which he was interested, the income of the trust still enjoyed exemption from tax because the income of the trust property was ultimately set apart for charitable purposes. In this way, the object of a trust as also the objects of granting exemption under the Income-tax Act, are being defeated.

It is submitted that if any charitable trust had invested, at any time during the previous year, in the shares or capital of an industrial or commercial undertaking, in which the donor was himself substantially interested, then the

dividends or share income from such investments should not be eligible for exemption and should be taxed in the hands of the trustees.

The study of tax treatment of charitable trusts abroad reveals that charitable trusts are subject to tax concessions almost in every country. In the United States of America, charitable contributions are subject to a ceiling which in case of individuals is 50 per cent of the individual’s net income for the year and in case of private foundations it should not exceed 30 per cent of the individual donor’s net income. Ceiling is also prescribed on corporate donors which is 10 per cent of donor’s net income. Not only this if the donor contributes more, he can carry forward his donation for five years and adjust the excess contribution against his succeeding year’s income.

All these healthy provisions can be incorporated in Indian tax system. Under section 80G, the ceiling prescribed for donations is 10 per cent of gross total income (exception apart). Looking to the needs of the society, it is submitted that there is need to give a fresh look to these provisions. To attract more donations, the ceiling be revised to 30 per cent of gross total income further, the carry forward provisions in the United States Law should be incorporated in the Indian law because an assessee who is to make more donations in one year, be not debarred of the benefit simply because he has exceeded the ceiling prescribed under the Act.

Further, as in the United States of America, donations to private foundations also qualifies for deduction out of the taxable income. In India, section 35AC of the Income-tax Act, 1961 has permitted public sector company, a local authority, an association or institution to undertake programmes as approved by the National Committee for Promotion of Social and Economic Welfare for carrying out any eligible project or scheme. As envisaged in the section, such organizations will have to use their own funds and will get 100
per cent deduction, therefor out of their income. Sometimes, the extent of their activities may be much larger and they may not have ample funds to achieve their target. It is, therefore, submitted that the private organisations should be permitted to have funds from other assessees only with the approval of the National Committee for Promotion of Social and Economic Welfare and contributions received by them should not only be exempt in their hands but the donor should be allowed 100 per cent deduction. The Committee should ensure that such funds are used for the purposes for which they are contributed. However, a ceiling for such contribution should be prescribed as is there in the United States of America.

Despite Government's keen desire for rural development, it has curtailed various avenues available earlier to the tax payers for their involvement in rural development programmes through the provisions of sections 35CC and 35CCA of the Income-tax Act. Earlier, these provisions provided for deduction of expenditure incurred on approved rural development programmes. To encourage participation by individuals and other assessees in rural development programmes section 35CCA allowed deduction of payment made to institutions engaged in approved rural development programmes.

Both these sections 35CC and 35CCA omitted by the Direct Tax Laws (Amendment) Act, 1987 with effect from 1st April, 1989. The Direct Tax Laws (Amendment) Act, 1989 has although restored the provisions of section 35 CCA, but has not modified the date of approval of rural development programmes.

It means, an assessee can only contribute to the National Fund for Rural Development set up by the Government and such contribution in case of an assessee engaged in the business or profession is allowed deduction under section 35CCA and other assessees under section 80GGA. With a view to give further impetus
to the assessees for involving directly or through approved institutions in rural development programmes, it is suggested that earlier provisions of sections 35CC and 35CCA be restored. By these provisions, assessees will be able to take up directly the programmes of rural development and also contribute to other institutions, which have the object of undertaking the programmes of rural development, of course, the Government will have the right to approve the programmes for rural development as also the institutions therefor.

Very recently, Tax Reforms Committee, commonly known as *Chelliah Committee* has made recommendations regarding deductions provided under sections 35AC, 35CCA, 35CCB, 80GGA, that the 100 per cent deduction allowable under these sections should be restricted to 50 per cent as in the case of deduction for other donations under section 80G. These recommendations, if implemented, will give a set back to those social welfare programmes which Government is trying, its level best, to implement by involving the business houses to invest their business profits, by giving 100 per cent deductions to them. At present, the Government, in order to promote investment of business profits in areas in which massive capital input is required for socio-economic development, has introduced a tax incentive scheme under section 35AC of the Income-tax Act allowing full deduction of donations made for such cases. Because of these tax incentive schemes, the response of companies, charitable trusts and voluntary organisations is overwhelming. The Government in its wisdom has rightly not implemented these recommendations of the *Chelliah Committee* while presenting the Finance Bill, 1992 on the floor of Parliament on 29th Feb 1992 though the recommendations made by the committee were available to the Government before finalising the Finance Bill, 1992. It is, therefore, suggested that the Government should vigorously pursue the implementation of the provisions contained in sections 35CCA and 35AC of the Income-tax Act, 1961.
As Government accords the highest priority to programmes of rural development and upliftment of weaker section to society, with a view to give further encouragement and information regarding tax incentives for the investment in social welfare programmes, it is suggested that the help of media can be taken for involving individuals, firms, companies, charitable trusts and voluntary organizations. Arrangement can be made for showing documentaries, interviews and advertisements on television network programmes. The newspapers can also help by publishing articles and providing maximum coverage regarding implementation of these programmes.

The present study reveals the complicacies of the provisions relating to charitable trusts, both in respect of incomes of the trust as well as donations to the trusts. Starting from a simple provision in the old Act of 1886, today the provisions relating to charitable trusts run into several sections, clauses, sub clauses which are more regulatory in character than fiscal. The fundamental questions, whether regulation of trusts should be through the Income-tax Act or through a separate enactment. It would seem to be desirable to enact a uniform central law, for controlling and regulating the working of various charitable and religious trusts, with the promptitude it deserves, particularly in the context of wide spread realisation that the trusts are being used as a medium of tax evasion and concentration of wealth in a few industrial houses. This uniform central law should govern registration of trusts, regulating their fund raising activity, maintenance of accounts, application of income, investment of trust funds, involvement of trusts in corporate affairs consequent on holding of shares in companies and providing for machinery to deal with the abuse of trust property.

Above all, this may contain all the regulatory provisions for proper management and control of public trusts. The Income-tax Act may merely
contain a provision for exemption if the Charity Commissioner has approved a particular charitable trust. Therefore, a comprehensive All India legislation is suggested for the purpose of controlling and regulating the working of various public charitable and religious trusts without any further loss of time.

Under the Uniform Central legislation the Government should have the power to nominate one or more trustees in case of trust with income exceeding a prescribed limit, notwithstanding the terms of the trust deed. The number of life trustees in any public trust should not exceed 25 per cent of the total strength of the trustees. As regards other trustees, the principle of rotation should be introduced so that one-third retire every five years. There should be yet another provision to ensure that the number of trustees who are close relatives of the founder of the trust, do not exceed 25 per cent, at any time, of the total strength of the trustees.

Keeping in view, the healthy points in Bomaby Public Trusts Act, 1950, The Andhra Pradesh Charitable and Hindu Religious Institutions Endowments Act, 1966 and Bihar Hindu Religious Trusts Act, 1950, a model of Charitable and Religious Trust Bill, has been prepared which contains the above said regulatory measures and is appended as Annexure III at the end of the present work.