

# Standards & NORMS

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## ANALYSIS OF DIRECT TAX CODE FOR NPOs

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### SUMMARY OF KEY ISSUES

**1.01** The proposed code has replaced the term 'Charitable Purpose' with 'Permitted Welfare activities'. Though the definition remains same but there is a radical shift in approach.

**1.02** The existing act provides for computing the exemption available to

NPOs, but the proposed code provides that the taxable income of an NPO shall be computed. Again there is a radical shift in treatment of NPOs from **exempt entities to tax paying entities**.

**1.03** The concept of different registration for NPOs under section 10(23C) and section

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12A have been deleted. There will be only one form of registration for all NPOs.

**1.04** The incentive u/s. 35AC which provide 100% deduction to the donors has been deleted. Under the proposed code the donors can get only 50% deduction on the donations.

**1.05** Religious trust or NPO have been kept out of the purview of the act. However they may have to get themselves registered under appropriate statutes.

**1.06** The benefits of 85% of application and 15% indefinite application has been deleted. The NPOs have to spend 100% of the funds during the year itself.

**1.07** The benefit of utilising unspent funds in the succeeding year under explanation to section 11(1) has been deleted. In other words if an NPO is unable to spend its funds during the year for reasons such as late receipt of fund, then the entire unspent amount will become taxable.

**1.08** The benefit of utilising unspent funds in the next five years u/s. 11(2) has been deleted. In other words if an NPO is unable to spend its funds during the year and it wants to apply the same in the next five years, it is not possible and the entire unspent amount will become taxable.

**1.09** The new code has proposed various new terms for assets, such as 'financial assets', 'investment assets' etc., which have not been defined from a NPOs perspective.

**1.10** The new code prohibits investments in 'financial assets'. This provision may imply that even creating FDRs may become difficult.

**1.11** The existing act allows exemption on all types of capital gain, provided the entire amount is reinvested in another

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asset. However the proposed code partially allows this benefit. The capital gain from financial assets will be subject to tax. It may be noted that it is not clear what a financial asset is.

**1.12** The existing act provides that all kind of capital expenditure are permissible if applied for the purposes of the NPO. The proposed code does not allow capital expenditures towards financial assets.

**1.13** The existing act allows depreciation as a valid expenditure. The proposed code has completely ruled out the possibility of claiming depreciation.

**1.14** The existing act allows accrual as well as cash basis of accounting. The proposed code prescribes only cash basis of accounting as well as admissibility.

**1.15** Under the existing act, by virtue of Supreme Court ruling in THANTI Trust case, even unrelated business activity is permissible. However the proposed code clearly provides that business can only be carried as a part of welfare activities.

**1.16** Under the existing act, the business activities of the 6th category NPOs are not permissible, i.e. NPOs engaged in advancement of any other general public utility. The same has been retained in the proposed code. This was totally unnecessary in the light of 1.15 above.

1.17 The existing act is silent but the proposed code provides that if an NPO convert itself into a commercial organisation then its entire networth will be taxed at the rate of 30%.

1.18 The existing act is silent but the proposed code provides that if an NPO fails to transfer, on its dissolution, assets to another NPO, then its entire networth will be taxed at the rate of 30%.

1.19 The existing act is silent but the proposed code provides that if an NPO ceases to be an NPO in the financial year and any two financial year out of the preceding four years, then its entire networth will be taxed at the rate of 30%.

1.20 Under the existing act expenditure outside India are permitted for specific purposes. The same has been retained in the proposed code. However under the existing act NPOs registered under section 10(23C) can have activities outside India, this provision is deleted.

1.21 Under the existing act there is no compulsion of having some activity during the year. The proposed code requires that NPO has to have welfare activity. If an organisation does not have welfare activity in three out of five years then the entire networth will become taxable.

1.22 Under the existing act businesses can be held as corpus assets. The proposed code does not allow any such benefits.

## **FROM CHARITABLE PURPOSE TO PERMITTED ACTIVITIES**

2.01 'Charitable Purpose' has been replaced by 'Permitted Welfare Activities' and therefore the emphasis is now on activities rather than only on intent. The new code has replaced the definition of

***If an NPO fails to transfer, on its dissolution, assets to another NPO, then its entire networth will be taxed at the rate of 30%.***

'Charitable Purpose' which is as under :

"Permitted Welfare Activity" means any activity,-

- (i) involving the relief of the poor;
- (ii) for the advancement of education;
- (iii) for providing medical relief;
- (iv) for the preservation of environment (including watersheds, forests and wildlife);
- (v) for the preservation of monuments or places or objects of artistic or historic interest; or
- (vi) for the advancement of any other object of general public utility;

2.02 The possible impact of this shift in nomenclature could be as under :

- (a) The existing Act talks about the intent or the purpose, the proposed code is mentioning 'activity'. In other words only intent will not be sufficient. For instance under the current provision even a clause about business activity in the memorandum may attract the provisions of Section 2(15). This may not be the case if the new code is enacted.
- (b) A very narrow view is being taken of the term 'Charitable Purpose'

by relegating it to welfare activities. It may create needless conflict and confusion, for example one may debate whether *Strengthening of Panchayats* or *Youth Leadership* is a welfare activity or not. Narrowing down the scope of the basic definition is totally unwarranted and is unlikely to serve any purpose from revenue's perspective.

- (c) There is radical shift by proposing discrimination within the gamut of welfare activities. The current act distinguishes between welfare activities and non welfare activities. The new code proposes to permit certain welfare activities, in other words certain activities may not be permitted even if they serve a welfare purpose.

### ***Suggested Way Forward***

**2.03** The proposed Act should distinguish between welfare and non welfare activities, rather than permitting few specified welfare activities.

## **FROM EXEMPTED INCOME TO TAXABLE INCOME**

**3.01** Under the existing Act the income which is **exempted** is required to be determined under Section 11(1). Under the proposed code the **taxable income** of charitable organisation is required to be computed under Section 87. There is a very fundamental and serious shift which brings charities on par with any other assessee. The existing section 11(1) begins with the

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*The existing act determines the exempted income but the proposed code will determine the taxable income.*

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wordings "...the following income shall not be included...." whereas the proposed section 87 says ".....the total income shall be computed.....". In other words, the existing act determines the exempted income but the proposed code will determine the taxable income.

**3.02** As a result all the existing regulatory provisions have been brought within the definition of NPO and therefore any default in complying even with the regulatory provision will put the organisation out from the purview of Chapter-IV.

**3.03** For the purpose of this chapter the income shall be calculated with reference to the gross receipts and gross outgoings instead of on the basis of commercial meaning of income. Hence for the purpose of computation of total income under Income Tax, Receipt and Payment account becomes the key financial statement instead of Income and expenditure account.

### ***Suggested Way Forward***

**3.04** The income of an NPO should be determined on a real basis considering the actual income during the year available for charitable purposes. The act should

determine the income for the purpose of computing legitimate exemptions rather than for determining the taxable income. It is unfair to determine the income of an NPO like a commercial organisations where income subject to tax is determined. The shift in computation method will cause needless hardship.

## **LEGAL OBLIGATIONS & RESTRICTED FUNDS**

**4.01** The new code is silent about the treatment of legal obligations and restricted funds received during the year. It may be noted that u/s 96(h) a legal obligation has been treated as a trust. In other words restricted grant bound by a contractual obligation, being a legal obligation, should be termed as a trust and should not form a part of the total income.

**4.02** However the new code provides that computation of income of NPO all receipts except loans and advances shall be considered as income. Therefore, restricted funds and legal obligations received during the year shall also be treated as income which is in contradiction with other provisions of the proposed code and also not sustainable legally.

### ***Suggested Way Forward***

**4.03** The process proposed for determination of income needs to be reconsidered. It is legally arbitrary to propose that all gross receipts (whether in the nature of income or not) shall be considered as a part of income. It is necessary to exclude legal obligations and contract bound fund received out of the purview of income.

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year.***

## **BRINGING ALL NPOs SUBJECT TO SIMILAR COVERAGE**

**5.01** Presently the charitable institutions are subject to tax either u/s. 10 or u/s. 11 but the proposed code eliminates all these distinctions and brings all organisations coming within the definition of NPOs under the coverage of chapter IV. Due to this suggested modification most of the institutions/funds which are presently enjoying the tax exemption status u/s. 10 may have to comply with chapter IV in line with other NPOs.

**5.02** Some of the entities which may be affected include:

<b>U/S.10</b>	<b>Name of the Institution</b>
Sub Sec.21	The scientific research association approved for the purpose of clause (ii) of sub-section (1) of section 35
Sub Sec.22B	News agency set up in India solely for collection and distribution of news as the Central Government may, by notification in the Official Gazette, specify in this behalf
Sub Sec.23A	An association or institution established in India having as

its object the control, supervision, regulation or encouragement of the profession of law, medicine, accountancy, engineering or architecture or such other profession as the Central Government may specify in this behalf, from time to time, by notification in the Official Gazette

Sub Sec.26AAB An agricultural produce market committee or board constituted under any law for the time being in force for the purpose of regulating the marketing of agricultural produce.

## **INCENTIVES TO DONORS**

**6.01** All the Donors' incentives have been clubbed and covered under section 72 of the direct tax code under the chapter Tax Incentives. It seems that present incentives under section 35 AC may not be available once the Direct Tax code becomes operational. The new code proposes three types of deductions to the donor :

- (i) 125% of amount donated
- (ii) 100% of amount donated
- (iii) 50% of amount donated

**6.02** However under the proposed provisions 125% benefit will be available only to research related institutions. 100% benefits is available to specified institution and 50% incentive is available to other institutions. In other words, NPOs have been deprived of the possibility of getting 100% privileges for the donor. As such the existing act was very harsh by providing only 50% deduction to the donor. Under the current provisions certain NPOs are provided registration under section 35AC, where the donor gets 100% benefits.

***The current legal scenario is not at all conducive for funds raising and resource mobilisation. The proposed direct tax code is a further setback in this regard.***

The current legal scenario is not at all conducive for funds raising and resource mobilisation. The proposed direct tax code is a further setback in this regard.

### ***Suggested Way Forward***

**6.03** There is an urgent need to put NPOs on par with other institution where 100% deduction is available to the donors. The current proposal of giving only 50% benefits to the donors is against the GOI National Policy on Voluntary Sector which promises to create an conducive and enabling environment for the NPOs.

## **STATUS OF RELIGIOUS TRUSTS**

**7.01** To our understanding Chapter IV applies to the organizations carrying on permitted welfare activities and does not cover the religious trusts.

**7.02** Moreover item No.38 of the seventh schedule exempts only :

*“any association, authority, body, institution or trust registered under any law of the Central, State or Provincial Government for the regulation of religious endowments.”*

**7.03** It implies that the religious endowments which are not registered under Central, State or Provisional Govt. may be subject to tax as these are neither covered under seventh schedule nor under Chapter IV. Therefore, religious organisations may have to get themselves registered under appropriate statute to get unconditional exemption.

***NPOs will have no right to formally accumulate and create funds for its sustainability. Currently NPOs are allowed 15% of their income as indefinite accumulation.***

### **100% APPLICATION OF FUNDS & SURPLUS SUBJECT TO TAX @15%**

**8.01** It is worthwhile to remember that the Finance Bill 2002 had proposed that all NPOs should apply 100% of their income during the year itself. Prior to that NPOs were required to apply only 75% of their income during the year. After considering representation from the civil society this harsh proposal was deleted and the Finance Act 2002 provided that NPOs should apply 85% of its income during the year. In other words, the direction to apply 75% of funds within the year was raised to 85%.

difficult even if they intend to apply 100% of their income. Now the unspent balance on cash basis is subject to tax @ 15%. Moreover there is no provision which allows carry forward and set off of deficit in any of the year and at the same time all the existing provisions for accumulation and options have been deleted.

### ***Suggested Way Forward***

**8.02** The proposed code has silently brought the same old proposal through the back-door. As per the new direct tax code 100% of income during the year has to be applied for charitable purposes. This proposal may have the following consequences :

**8.03** There is an urgent need to reconsider the provision of 100% application, it may result fatal for the NPO sector. An NPO can not receive any grant which is to be implemented over a period in excess of 1 year. The existing provision of 85% application during the year and the flexibility to spend income over a period of 5 years should be retained. It is practically infeasible to apply 100% of the income during the year itself.

- (i) NPOs will have no right to formally accumulate and create funds for its sustainability. Currently NPOs are allowed 15% of their income as indefinite accumulation. And accumulation for five years is permitted for unspent fund beyond 15%.
- (ii) NPOs receiving funds towards the end of the year may find it

**8.04** Further the code provides that all receipts except corpus donation or loans should be applied 100% during the year. For instance even membership fee or life membership fees received have to be applied 100% during the year. Such provision are unfair and should be reconsidered.

## CONCEPT OF FINANCIAL ASSET

**9.01** The new direct tax code has thrown various new concepts of assets, which are :

- (i) Financial asset
- (ii) Investment asset
- (iii) Capital Expenditure (asset)
- (iv) Business capital asset
- (v) Business held as asset

**9.02** None of the above have been defined from a NPO perspective. For instance “investment asset” has been defined as any capital asset which is not a business capital asset. The financial assets have not been defined. We are more used to the terms such as ‘project assets’ or ‘corpus assets’ rather than the proposed commercial jargons.

**9.03** The term financial asset is not defined but the purported purpose seems to be to deprive the NPOs from keeping available project funds in liquid assets such as FDRs and other instruments. Because section 90(e) specifically provides that any investments in financial assets shall not be treated as valid application of funds. In other words the unspent balances at the end of the year shall not be treated as application if converted into financial assets. Further, because of the prohibition even creating short term deposits within the year, might not be permitted which is totally irrational and unfair.

**9.04** Similarly we have to wait for the explanation regarding other assets in context of NPO. But on the face of it seems that needless and controversial concepts are being created in the name of simplification. For instance it is difficult to understand why and how an NPO should distinguish between an investment asset and a financial asset.

*The purported purpose seems to be to deprive the NPOs from keeping available project funds in liquid assets such as FDRs and other instruments.*

### *Suggested Way Forward*

**9.05** Needless and complicated concepts of assets should not be created. NPOs should be allowed the legitimate authority to invest its balances in financial assets. The investment in financial assets should not be subjected to tax. NPOs should be provided the right to spend funds on projects across the years. The proposed provision are against the principle of natural justice and are not conducive for any sustained welfare activities.

## CORPUS & OTHER LONG TERM GRANTS

**10.01** The receipt towards Corpus Fund has not been exempted from gross receipt u/s. 89(2), it has been covered as an payment in section 90, meaning thereby all the contributions towards corpus first has to be added as receipt and then should be considered as outgoing.

**10.02** It may also be noted that a corpus donation is the only possibility of accumulating funds towards sustainability or reserves. All other accumulation can happen only after payment of taxes at prescribed rate, currently it is proposed at 15%.

### ***Suggested Way Forward***

**10.03** Corpus donations should not be considered as a part of gross income at all. Because the same amount is allowed as deduction again. It creates an needless illusion of income which is not there. Further all other long term grants and legal obligations should also be allowed to the excluded from the purview of gross receipts. Under the proposed provision there is no scope for receiving endowment or long term project grant.

### **CAPITAL GAINS**

**11.01** Presently the capital gains on transfer of **capital assets** are chargeable to tax u/s. 11(1A) of the Income Tax Act, 1961 which provides for benefits of roll over i.e. if the net consideration is utilized in acquiring the new capital asset, then capital gain arising from the transfer shall deemed to have been utilized.

**11.02** However the proposed code distinguishes between capital assets. According to the new code capital assets other than financial assets may avail capital gain benefit by using the entire sale proceed in purchase of another asset other than financial asset or using it for permitted welfare activities.

**11.03** The capital gain on transfer of **financial asset** shall be computed as per provision of section 44 - 53.

**11.04** There is no radical shift in the treatment of capital gain regarding assets other than financial assets. However the code proposes to make capital gain from financial assets subject to tax. It may turn out to be a very harsh and irrational provision though we still not know what a financial asset means. It seems that all liquid assets created out of unspent

***For the purposes of capital gain the distinction between financial assets and other assets should be removed.***

balances and other general balances may be treated as financial assets.

**11.05** The new code is trying to distinguish between investment assets and financial assets which is highly unusual and it remains to be seen how this distinction and disparity in treatment is illustrated.

### ***Suggested Way Forward***

**11.06** For the purposes of capital gain the distinction between financial assets and other assets should be removed. Any asset irrespective of its nature should be allowed to be reinvested in case of sale and capital gain. Otherwise the capital and resources of the NPOs will eroded. This provision is particularly harsh when the possibility of accumulation and resource mobilisation of funds has also been plugged.

### **ALLOWABILITY OF CAPITAL EXPENDITURES**

**12.01** As per the new code permissible outgoings includes:

- Amount actually paid towards capital expenditure for the purpose of business

- Amount actually paid in relation to investment asset, not being a financial asset

Therefore as per section 90 of the new code it seems that capital expenditure actually paid towards investment assets is treated as valid application. One only hopes that the investment assets include project assets and other assets purchased towards fulfillment of the objectives.

### ***Suggested Way Forward***

**12.02** With regard to capital expenditures there is a need clarify that all capital expenditures for the purposes of welfare activities and towards attainment of the objectives of the society shall be permissible. The prohibition against creation of financial asset should be deleted because creation of a financial asset out of project fund is any case not treated as valid application of funds.

## **ISSUE OF DEPRECIATION**

**13.01** Presently depreciation is totally allowed as expenditure. Under the current provisions even depreciation on those assets which are already treated as expenditure is also permissible. However, such allowability is judicially debatable and various High Courts have ruled in favour of the NPOs. In other words, under the existing provisions depreciation is permissible.

**13.02** The proposed code has completely ruled out the possibility of claiming depreciation as an expenditure because only cash expenditures are permissible. This is again a unbelievably harsh provision because it will result in natural erosion of the corpus and networth of the NPOs without any protection of depreciation

***The code has completely ruled out the possibility of claiming depreciation as an expenditure as only cash expenditures are permissible***

deduction which is available to other assesseees.

### ***Suggested Way Forward***

**13.03** There is an urgent need to consider depreciation of assets as a valid expenditure. It is against all accounting principles and also principles of natural justice to deny depreciation which is an inevitable expenditure. The proposed code if enacted will result in erosion of the networth of NPOs due to efflux of time and project activities if depreciation is not permitted as expenditure.

## **BUSINESS ACTIVITY OF AN NPO**

**14.01** Presently the incidental business activity is allowed under the Income tax Act for the specified category of NPOs.

**14.02** However the proposed Code has restricted the coverage of incidental business activity and has allowed only those business activities which are carried on while actually undertaking the welfare activities. In other words, the ruling of Supreme Court in *Thanti Trust case* would stand nullified. Just to remind, in this case Supreme Court ruled that even unrelated activities will be treated as incidental provided the entire income is used for charitable purposes. This is a proposal in

the right direction. However, after this change there is no need to deprive the sixth category NPOs from engaging in business activities. The current law and the proposed code prohibit business activities in case of NPOs engaged in 'Advancement of any other general public utility'.

**14.03** Now since the new code has redefined the incidentality of business as a result no NPO can engage in unrelated business activities. Therefore, there is no need for prohibiting one category from engaging in business activity. Because in any case all categories of NPOs have to engage in incidental business activities. If the business activity is incidental then there is no reason why all NPOs shall not have the benefit.

#### ***Suggested Way Forward***

**14.04** The direct tax code has already taken a understandable step by providing under section 96 that business shall be treated as incidental only if it is carried on in the course of implementing welfare activities. After this amendment there is no need to deprive NPOs engaged in 'Advancement in any other object of general public utility' from engaging in incidental business activities.

### **EXEMPT INCOME AS PER SIXTH SCHEDULE**

**15.01** As per section 9 of the code, total income for a financial year of any person shall not include any of the income mentioned in the Sixth Schedule. It may be noted that the Sixth Schedule specifies various exempt incomes including agricultural income. Such income shall not be considered as a part of income and

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has redefined the  
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business activities***

therefore should not be subject to 100% application during the year.

**15.02** The term 'person' defined under the act includes Non-Profit Organisation. Hence the income mentioned in Sixth Schedule should also be exempt even in the hands of NPO.

### **DETERMINATION OF BUSINESS INCOME**

**16.01** In case of NPOs doing business activity it is not clear how the computation will be made. There is no provision for applicability of Section 28 to 43 while computing income from Business. Therefore, it seems that the business income of NPOs shall be determined on normal commercial principles without referring the provisions under the chapter of business income.

**16.02** Moreover, the gross receipts from the permitted welfare activities include income derived from business and the outgoings include the expenditure of capital nature incurred for the purpose of business. Hence, it seems that the present provision as per chapter IV does not intend to apply section 28 to 43 while computing income from business.

## CONVERSION OF AN NPO INTO COMMERCIAL ORGANISATION

**17.01** Under section 94 it is provided that if the NPO found to be in any one of the three circumstances :

- (i) Converts itself into an organisation which does not qualify for exemption
- (ii) Ceases to be an NPO in the financial year and any two financial year out of the preceding four years.
- (iii) Fails to transfer, on its dissolution, assets to another NPO.

then the NPO shall be liable to be taxed at the rate of 30% of its net worth.

**17.02** This provision seems to be out of context and very harsh. As it proposes to tax the entire networth accumulated over the years. It may be noted that accumulated networth is never considered as income. For some assesseees, it may be subject to wealth tax but not income tax. Therefore, something which normally is not within the purview of income should not be subjected to tax at maximum marginal rate. Further all surpluses are subject to tax at 15%, therefore, a portion of the networth will be created out of income which has already been taxed. Taxing such income again will result in double taxation.

**17.03** It may further be noted that such provisions will be attracted if the NPO is not allowed exemption in three financial years. In other words such NPO would have already paid taxes on the entire income during these years and again the networth will be subjected to tax, which will result in double taxation.

**17.04** The NPOs who once enjoyed total exemption now will be subjected to double

*After the enactment of the code NPOs of national importance will not have the privilege of doing international activities of their choice.*

taxation, this is the enabling environment proposed by the new code.

### **Suggested Way Forward**

**17.05** There is an urgent need to reconsider the provision pertaining to taxation in case where an NPO ceases to be an NPO for income tax purposes. It is proposing 30% tax of the networth. This provision is very harsh particularly when all surpluses (which go on to make networth) are already subject to 15% tax.

## EXPENDITURES INCURRED OUTSIDE INDIA

**18.01** The present Act under section 11(1)(c) provides that the application of income outside India shall be permissible only if it tends to promote international welfare in which India is interested. There seems to be a similar provision u/s. 90(g) of the code. Therefore, it seems that for international activities *status quo* is maintained. However, it may be noted that NPOs of national importance registered under section 10(23C) were permitted to do international activities. In other words, after the enactment of the code NPOs of national importance will not have the privilege of doing international activities of their choice.

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### ***Suggested Way Forward***

**18.02** This provision needs reconsideration as many NPOs work on global causes and have international networks. Therefore, depriving them from doing international activities would be highly detrimental to them and not desirable in our national interest as well.

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***This provision of taxing the entire networth at the rate of 30%, if the NPO does not have activities, needs to be reconsidered.***

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### **COMPULSORY ACTIVITY EVERY YEAR**

**19.01** The proposed code u/s. 96(d)(v) provides that all NPOs are compulsorily required to have welfare activities every year. If an NPO does not have welfare activity then it will not be considered as an NPO for that year. Further, if such NPO does not have activity in two out of four preceding years then its entire networth will be subjected to tax at the rate of 30%.

commercial / business property. However after the enactment such trust and practices shall not be permitted.

### ***Suggested Way Forward***

**20.02** The NPOs should be allowed to hold business as corpus assets and legal obligations which is permissible under the current act.

### ***Suggested Way Forward***

**19.02** This provision of taxing the entire networth at the rate of 30%, if the NPO does not have activities, needs to be reconsidered. Because NPOs, generally, depend on external grants and assistance and it is likely that might not be any activity in some year.

### **SUMMARY OF SUGGESTED WAY FORWARD**

**21.01** The proposed Act should distinguish between welfare and non welfare activities, rather than permitting few specified welfare activities.

### **HOLDING BUSINESS AS CORPUS ASSETS**

**20.01** The current Act for needs NPOs to hold business as corpus assets. The proposed code u/s. 95(a)(i) provides that NPOs can not hold business as corpus assets. For instance under the current law it is possible to create a trust by settling a

**21.02** The income of an NPO should be determined on a real basis considering the actual income during the year available for charitable purposes. The act should determine the income for the purpose of computing legitimate exemptions rather than for determining the taxable income. It is unfair to determine the income of an NPO like a commercial organisations where income subject to tax is determined. The shift in computation method will cause needless hardship.

**21.03** The process proposed for determination of income needs to be reconsidered. It is legally arbitrary to propose that all gross receipts (whether the nature of income or not) shall be considered as a part of income. It is necessary to exclude legal obligations and contract bound fund received out of the purview of income.

**21.04** There is an urgent need to put NPOs on par with other institution where 100% deduction is available to the donors. The current proposal of giving only 50% benefits to the donors is against the GOI National Policy on voluntary sector which promises to create an conducive and enabling environment for the NPOs.

**21.05** There is an urgent need to reconsider the provision of 100% application, it may result fatal for the NPO sector. An NPO can not receive any grant which is to be implemented over a period in excess of 1 year. The existing provision of 85% application during the year and the flexibility to spend income over a period of 5 years should be retained. It is practically infeasible to apply 100% of the income during the year itself. Further the code provides that all receipts except corpus donation or loans should be applied 100% during the year. For instance even membership fee or life membership fees received have to be applied 100% during the year. Such provision are unfair and should be reconsidered.

**21.06** Needless and complicated concepts of assets should not be created. NPOs should be allowed the legitimate authority to invest its balances in financial assets. The investment in financial assets should not be subjected to tax. NPOs should be provided the right to spend funds on projects across the years. The proposed provision are against the principle of natural justice and are not conducive for any sustained welfare activities.

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***Corpus donations should not be considered as a part of gross income at all. Because the same amount is allowed as deduction again.***

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**21.07** Corpus donations should not be considered as a part of gross income at all. Because the same amount is allowed as deduction again. It creates an needless illusion of income which is not there. Further all other long term grants and legal obligations should also be allowed to the excluded from the purview of gross receipts. Under the proposed provision there is no scope for receiving endowment or long term project grant.

**21.08** For the purposes of capital gain the distinction between financial assets and other assets should be removed. Any asset irrespective of its nature should be allowed to be reinvested in case of sale and capital gain. Otherwise the capital and resources of the NPOs will eroded. This provision is particularly harsh when the possibility of accumulation and resource mobilisation of funds has also been plugged.

**21.09** There is an urgent need to consider depreciation of assets as a valid expenditure. It is against all accounting principles and also principles of natural justice to deny depreciation which is an inevitable expenditure. The proposed code if enacted will result in erosion of the networth of NPOs due to efflux of time and project activities if depreciation is not permitted as expenditure.

**21.10** The direct tax code is already taken a very desirable step by providing under

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section 96 that business shall be treated as incidental only if it is carried on in the course of implementing welfare activities. After this amendment there is no need to deprive NPOs engaged in 'Advancement in any other object of general public utility' from engaging in incidental business activities.

**21.11** There is an urgent need to reconsider the provision pertaining to taxation in case where an NPO ceases to be an NPO for income tax purposes. It is proposing 30% tax of the networth. This provision is very harsh particularly when all surpluses (which go on to make networth) are already subject to 15% tax.

**21.12** This provision needs reconsideration as many NPOs work on global causes and have international networks. Therefore, depriving them from doing international activities would be highly detrimental to them and not desirable in our national interest as well.

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***The NPOs should be allowed to hold business as corpus assets and legal obligations which is permissible under the current act***

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**21.13** This provision of taxing the entire networth at the rate of 30%, if the NPO does not have activities, needs to be reconsidered. Because NPOs, generally, depend on external grants and assistance and it is likely that might not be any activity in some year.

**21.14** The NPOs should be allowed to hold business as corpus assets and legal obligations which is permissible under the current act.

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