

1. THIS CODE TREATS LARGE PUBLIC TRUST AND SMALL ORGANISATIONS ALIKE

This code is applicable to all organizations operating as not-profit entities, which can range from foundations, NGOs, Research and advocacy organizations, charity hospitals, etc. Whether they are providing health or livelihood related services to the marginalized in remote villages, or conducting research based advocacy, printing popular publications for public awareness, charging nominal user fee to provide sustainability to community initiative. Unfortunately, this code puts large public (Ports, Religious, public schools, corporate hospitals) trusts and small organizations in one category.

2. UNFAIR AND INCONSISTENT PROCEDURE FOR DETERMINING INCOME

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 shift, which brings charities on par with any other assesses.

The proposed method of computing taxable income is legally incorrect because in case of NPOs the gross receipt of 'voluntary contributions' itself is income for income tax purposes. Therefore, it is appropriate that exemptions are allowed only if it is expended in specified manner. It need to be kept in mind that under the existing law NPOs are required to spend, income which otherwise would have been taxable, in prescribed manner. Section 284(124)(g) defines 'voluntary contribution' as a part of income; any further deduction to such income will be in contradiction of the proposed code itself. Hence the existing manner of determining the exempted income is appropriate for NPOs.

It is suggested that the existing procedure of first determining the taxable income and then determining the exempted income should be retained. The proposed procedure of arbitrarily and artificially determining the income of NPOs should be deleted.

3. UNFAIR TO TREAT ALL RECEIPTS AS INCOME

The proposed code provides that all receipts (except loans) whether income or not shall be treated as income which is unfair and unconstitutional. It is also in direct contradiction with section 284(124) of the proposed code, which defines income. If the proposed code becomes law then the following receipts, which cannot be considered as income under any law, shall be treated as income:

- Receipt towards share capital or life membership fee
- Legal obligations and Restricted Grants etc

It may also 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.

The proposed code should suitably clarify and exclude those receipts, which cannot be considered as income, even under the mandate of the proposed code. For example, it should exclude legal obligations and restricted grants, receipts towards share capital, life membership fees etc.

4. 100 PERCENT APPLICATION OF INCOME DURING THE YEARS

The new direct tax code provides that 100 percent of income during the year has to be applied for charitable purposes which is practically not feasible and therefore, unfair. The problems which the NPOs may face could be:

- Receiving funds towards the end of the year.
- Receiving funds for 2-3 years together
- 100 percent application would imply no reserves or savings for contingencies.

The proposed code should retain the existing option of applying the income in the next year or over next 5 years. It is not possible to apply 100 percent of the income during the year itself. It may be noted that up to 2002 only 75 percent of income was required to be applied and currently 85 percent of income is required to be applied during the year.

5. 15 PERCENT ACCUMULATION WITHDRAWN

The Code proposes to withdraw the benefit of saving 15 percent of income every year. Currently NPOs are allowed 15 percent of their income as indefinite accumulation. Such accumulation provides a limited benefit to the NPOs for creating reserves for its future sustainability. NPOs depend on external donations and grants and have little possibility for creating reserves for future. The existing Act is permitting a very modest 15 percent accumulation for future sustainability.

It is necessary that an enabling law is created for the NPO sector to sustain itself. The withdrawal of 15 percent indefinite accumulation will strangle the sector and have a serious impact on the future sustenance of the NPOs. Therefore, the existing provision of 15 percent indefinite accumulation should be retained.

6. UNFAIR TO DISALLOW DEPRECIATION

Presently depreciation is totally allowed as expenditure. The proposed code has completely ruled out the possibility of claiming depreciation as expenditure because only cash expenditures are permissible. This is again an unbelievably harsh provision because it will result in natural erosion of the corpus and net worth of the NPOs without any protection of depreciation deduction which is available to other assessee. Since the proposed code is considering only cash outflow and inflow various other non-cash expenditures shall also not be considered.

It is unfair to disallow depreciation to the NPO sectors which is available to all other assessee. The Proposed code should clarify and ensure that the net worth of the NPOs is not needlessly eroded. Therefore, depreciation should be allowed as a legitimate expenditure.

7. TAX ON SURPLUS

Though surplus of one year will be taxed, it may be difficult for the NGOs to bring forward deficit of a past year, and set it off against the surplus. Thus, if we spend borrowed money for a project, we may end up paying tax when the grant is actually received next year.
