

27th January, 2009

PRE-BUDGET MEMORANDUM

**Dr. Manmohan Singh
Hon'ble Prime Minister
Parliament House No.10
New Delhi -110001**

Respected Sir,

On behalf of Voluntary Action Network India (VANI) a network of 2200 voluntary organisations engaged in diverse fields of social and economic development of a charitable nature, we the undersigned make the following submissions:

1. That the Government and the society at large has recognised the valuable services being rendered by the voluntary organisations in the field of education, health, poverty alleviation, conservation of environment, assistance to physically and mentally challenged persons and other marginalised and weaker sections of the population across the country and especially in remote regions inhabited by tribal's.
2. That in recognition of this position, the Government of India has formulated a comprehensive **National Policy for the Voluntary Sector** in which government and voluntary sector partnership is accorded a priority in social and economic development in implementation of various schemes and programmes.
3. That VANI has carried out an intensive consultation with its partners and associate voluntary organisations in understanding the practical problems faced by them in their day to day operation in the matter of compliances with Income Tax Laws and rules made there under, and based on the views expressed in these consultations, following issues pertaining to the administration of the Income Tax Laws are placed here under with suggestions for changes:

In the following pages are the key issues which we would like the Ministry of Finance to consider while drafting the Budget for year 2009:

CHANGE IN DEFINITION OF CHARITABLE PURPOSE AND BUSINESS INCOME OF NGOs

The Finance Act, 2008 w.e.f. 1-4-2009 has amended the definition of 'charitable purpose' under section 2(15) which have far reaching implications on the voluntary sectors. An explanatory Circular No. 11/2008, New Delhi, the 19th December, 2008; F. No.134/34/2008-TPL, has also been issued in this regard. However, there are some serious concerns which need immediate and urgent attention:

- (i) **A Gandhian rural NGO is now a commercial entity** : The definition of 'charitable purpose' is divided into 4 parts, viz. (i) relief of poor, (ii) education, (iii) medical relief, (iv) advancement of any other object of general public utility. The Finance Act, 2008 w.e.f. 1-4-2009 has excluded the fourth limb organisations i.e. advancement of any other object of general public utility, from engaging in any trade, commerce or business related activity. The NGOs exclusively engaged in the field of education, medical relief and relief of poor will not be hit by this amendment. There is an unqualified and open prohibition of incidental business activities only for the fourth limb NGOs. This will affect many genuine NGOs where such activities are an integral part of their development work. For example, a small Gandhian NGO which works on the principle of Swaraj and manufactures and sells indigenous products will be treated as a commercial entity. There is an immediate necessity to provide clarification on the implication of this amendment. The above mentioned explanatory circular has also not provided the activities which should not be considered as business in context of NGOs.
- (ii) **Presumptions that there are commercial and masked entities only in the fourth limb and not in the field of education and medical relief** : NGOs exclusively engaged in the field of education, medical relief and relief of poor shall not be hit by this amendment. The stated legal intent behind this amendment is to prevent commercial entities from misusing the exemptions available to genuine charitable organisations. This legal intent is highly appreciated and would provide great relief to the sector if commercial entities and vested interests are weeded out. However, the amendments defeat the very purpose and intent, because commercial and masked entities might be there in all categories of NGOs. Violation or misuse of law can happen in any category of NGOs. In fact the medical and educational institutions are the one where instances of commercialisation are more apparent. Last year in court cases educational institutions were held to be commercial in nature and therefore, 12A status was revoked. In such circumstances the ideal way would have been to develop a mechanism to identify masked and unscrupulous entities in all categories of NGOs. The current law allows business activities to the first three type of NGOs and surprisingly even incidental business activities are not permissible for the fourth limb NGOs.

- (iii) **A masked entity is not entitled to exemptions even without the amendments:** A masked entity (the term used in the explanatory circular issued by the CBDT) is in any case not entitled to any exemptions. A generic change in law cannot prevent fraudulent practices. The current amendments under the apprehension that there might be some masked entities have deprived most of the genuine NGOs from doing various kinds of charitable and incidental activities. For instance, marketing the handicrafts prepared by the beneficiaries and communities will render an NGO commercial in nature.
- (iv) **The amendments are discriminative in nature against constitutional rights:** The amendments have provided privileges to the first three category of NGOs without clarifying why they deserve such privileges. And it deprives the fourth category of NGOs which happens to be the residual category, in other words it is the category where all other NGOs shall be covered. Therefore, the residual category cannot be considered as an class in itself. From a Gandhian khadi unit to Chambers of Commerce anything can come under this category. As per constitutional provisions and judicial precedence it has been held that discriminative law has to come against or in favour of a specific class with specific reasons. The impugned amendment fails on both counts.
- (v) **The activities which can be considered as charitable not clarified:** The Hon'ble Finance Minister had promised on the floor of the Parliament that genuine NGOs will not suffer and their concerns shall be addressed through an explanatory circular. On 19th December 2008, an explanatory circular was released, but this circular does not talk about the activities of various genuine NGOs which might get entangled in the search for masked entities. It is very important to clarify that various activities as detailed below shall not be considered as business activities:
- SHG group formation and micro-finance
 - Consultancy on charitable and development work related issues.
 - Income from properties and infrastructure.
 - Marketing indigenous and other products manufactured by beneficiaries and communities, etc.

Income generation and self-reliance is something fundamental to the existence and survival of an NGO,

therefore, these amendments needs to be immediately revisited.

- (vi) **The applicability of the amendments is very harsh:** Under the current provisions even an insignificant amount of incidental business activity will result in forfeiture of the entire exemptions. It is very unfair and harsh, rather only the business income should be brought to tax. The government should also consider setting a limit or percentage upto which incidental business activities can be conducted.
- (vii) **The amendments are open ended and far reaching:** Under the current provisions even a small rural NGO with, say, less than 5 lakh turnover working on Gandhian principle, manufacturing indigenous products will be treated as commercial organisation. It is desirable that a base limit of around 50 lakh should be fixed upto which the NGOs shall be exempted.

Keeping the above in view, we would request you to kindly reconsider the above proposed amendment to encourage the civil society organizations engaged in genuine charitable work.

With best wishes,

Very truly yours,

Paresh Tewary, Chief Executive Officer, **Voluntary Action Network India.**

Anand Kumar, General Manager (Operations), **Commonwealth Human Rights Initiative**

Anil Goel, Head, Finance, **CAF India**

Ashok K Seth, Senior Finance Manager, **Plan International**

Babykutty Ninan, Finance Manager, **Christian Medial Association of India**

Gita Kavarana, Head Institutional Development, **Centre for Science and Research**

Jayant Kumar, Head of Programmes, **Church's Auxiliary for Social Action (CASA)**

Karta Singh, **Women Power Connect**

K.K. Jaswal, Director, **Commoncause**

Mamta Srivastava, Programme Manager, **Indian Alcohol Policy Alliance**

Manoj Fogla, **Chartered Accountant, DM Associates**

Mathew Jose, Head, Finance, **Deepalaya**

Ninan Oomen, Ex- Executive Director, **William Carey Study and Research Centre**

Pallavi Kumar, CEO, **South Asian Fund Raising**

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Sudeep Biimbrawh, **Plan India**

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Vikrant Mahajan, Chief Operating officer, **Sphere India**

Yamini Mishra, Executive Director, **Centre of Budget and Governance Accountability**