

# AuditAble

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### Intention

What does the Department want to achieve from this change? During his speech, the Honorable Minister for Finance stated:

“Charitable purpose” includes relief of the poor, education, medical relief and any other object of general public utility. These activities are tax exempt, as they should be. However, some entities carrying on regular trade, commerce or business or providing services in relation to any trade, commerce or business and earning incomes have sought to claim that their purposes would also fall under “charitable purpose”. Obviously, this was not the intention of Parliament and, hence, I propose to amend the law to exclude the aforesaid cases. *Genuine charitable organisations will not in any way be affected.*

[emphasis added]

The Memorandum accompanying the budget proposals provides more detail:

“...It has been noticed that a number of entities operating on commercial lines are claiming exemption on their income either under section 10(23C) or section 11 of the Act on the ground that they are charitable institutions. This is based on the argument that they are engaged in the “advancement of an object of general public utility” as is included in the fourth limb of the current definition of “charitable purpose”. Such a claim, when made in respect of an activity carried out on commercial lines, is contrary to the intention of the provision.

With a view to limiting the scope of the phrase “advancement of any other object of general public utility”, it is proposed to amend section 2 (15) so as to provide that “the advancement of any other object of general public utility” shall not be a charitable purpose if it involves the carrying on of -

(a) any activity in the nature of trade, commerce or

business or,  
(b) any activity of rendering of any service in relation to any trade, commerce or business, for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity, or the retention of such income, by the concerned entity.

This amendment will take effect from the 1st day of April, 2009 and will accordingly apply in relation to the assessment year 2009-10 and subsequent assessment years.”



## *Trade, Commerce and Business*

A key phrase in the proposed amendment is 'trade, commerce or business'. Let us look at these three words more closely:

### **1. Business**

This word has been defined in section 2(13):

“Business” includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture’.

### **2. Trade and Commerce**

The word 'trade' is not defined in the Act itself. Black's Law Dictionary defines trade as 'the business of buying and selling or bartering goods or services'. It goes on to say that 'trade and commerce' refers to 'every business occupation carried on for subsistence or profit and involving the elements of bargain and sale, barter, exchange, or traffic’.

We can clearly see three elements, which have also been emphasized in judicial interpretations of these words:

1. Repetitiveness of activity
2. Exchange
3. Subsistence or profit

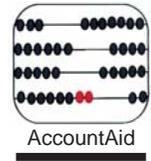
### **The Problem of Profit**

Curiously, the definition of business in section 2(13) makes no reference to the purpose of the activity, such as livelihood or profit. This may have been done to avoid litigation, as purpose or intention cannot be so easily established from the activity itself.

However, this creates a problem when we compare not-for-profit activities with business activities. If the activities are similar (e.g. selling of greeting cards) in appearance, then the law will not be able to distinguish between the two activities, on the basis of deeper purpose. It will not matter that one of the groups is providing public benefit with the surplus, whereas the other is just earning a livelihood.



**‘Trade and Commerce’ refers to ‘every business occupation carried on for subsistence or profit and involving the elements of bargain and sale, barter, exchange, or traffic’.**



## Implications

This will mean that certain charitable organizations, which have business-like activities, will be denied tax exemption from the coming financial year.

This move will not affect schools or hospitals, or organizations which work for relief of the poor. Religious organizations will also not be affected, unless they have taken exemption as a charitable organization.

However, other charitable organizations will be hit hard, if they have any business-like activities, or charge any fees or consideration from others. This could even cover cases where an NGO publishes a magazine and charges subscription fees or accepts advertisements for money.

This may include the following kind of organizations:

1. Training organizations
2. Resource organizations
3. Human Rights organizations
4. Micro-credit organizations
5. Environmental organizations
6. Advocacy organizations
7. Research organizations
8. Chambers of Commerce

9. Professional associations
10. Fund-raising organizations
11. Networking organizations, etc.

If the amendment goes through, there will be two options for such organizations:

1. Give up any activities which can be seen as trade, business or commercial, or
2. Show that they are only working for relief of poor or are only running schools or hospitals.

If they cannot do either of the above, they may have to prepare to pay income tax from the coming financial year.

## Conclusion

The new amendment will end the distinction between for-profit and not-for-profit activity for a large number of NGOs. The non-traditional NGOs are more likely to be affected. At the very least, they will need to prove to the Assessing Officers that their activities do not constitute 'trade, commerce or business'.

This is at variance with the Honorable Minister's promise to the Parliament that 'genuine charitable organisations will not in anyway be affected'.

