CHAPTER - III
LEGAL ASPECTS OF NON – GOVERNMENT ORGANIZATIONS

3.1 LEGISLATION IN NGOs:
In India, NGO can be formed and registered under various legal identities: a Charitable Trust, a Society under the Societies Registration Act and a Company under Section 25 of the Companies Act of 1956.

Different states in India have different Trusts Acts in force. In case, there is no Trust Act in any state, the general principles of the Indian Trusts Act1882 are applicable. In state of Maharashtra and Gujarat, Bombay Public Trusts Act, 1950 is applicable.

Societies are registered under the Societies Registration Act, 1860, which is a federal act. In certain states, which have a charity commissioner, the society should be registered under both the Acts; the Societies Registration Act and Bombay Public Trusts Act.

Section-25 companies are registered under section-25 of the Indian Companies Act. 1956.

3.2 REGISTRATION METHODS OF NGOs:

Trust: A public charitable trust is usually floated when there is property involved, especially in terms of land and building.1

“The main instrument is the trust deed. The three parties (settler, trustee and beneficiary of trust) are linked by a trust deed. Trusts are commonly classified as private/family and public trusts. The main difference between a private and public trust is that while the beneficiary of a private trust is one or a few individual (mostly family members of the donor), the beneficiary of a public trust is the general public. For the purposes of forming an NGO ensuring public benefit a public trust can be formed.”2

The trust deed should include – name of the trust, trustee, settler and beneficiary, objectives of the trust, procedure for appointment, removal or replacement of a trustee and any other condition that the settler may wish to enforce.
Important features of Trust:
- A trust can be established by two or more individuals and registered under the Trusts Act of the State.
- Legal requirements of a trust are simpler than that of section 25 company.
- Board of trustees are responsible for management of trust and they can remain so for life long and cannot be removed by election as the case is in society.
- The disadvantage is that the alteration of the objects laid down in the trust deed is difficult and only the settler can modify them.
- It is difficult to wind up a trust.

Society: A society is association of people who come together for some common purpose and do the work that is useful to others.

According to section 20 of the Societies Registration Act, 1860, the following societies can be registered under the Act: ‘charitable societies, military orphan funds or societies established at the several presidencies of India, societies established for the promotion of science, literature, or the fine arts, for instruction, the diffusion of useful knowledge, the diffusion of political education, the foundation or maintenance of libraries or reading rooms for general use among the members or open to the public, or public museums and galleries of paintings and other works of art, collection of natural history, mechanical and philosophical inventions, instruments or designs’

The main instrument is ‘Memorandum of Association’ and ‘Rules and regulations’. The memorandum of association contains- name of the society, the registered/ principal office of the society, objectives of the society, names, addresses and occupations of the members of the governing body. The rules and regulations direct the members of the governing body to carry out internal management and functions of the society.
Important features of Society:
- The legal requirements are much simpler than in the case of a trust or Section 25 companies.
- Unlike trusts, a society has a more flexible and democratic set up with membership and an elected body to manage the society.
- It is easier to wind up a society than it is to wind up a trust.
- Legal requirements of a society are simpler than that of section 25 company.

Company licensed under Section 25 of the Companies Act of 1956: A non-profit company can be formed by people for non-profit activity. According to section 25(1)(a) and (b) of the Indian Companies Act, 1956, a section-25 company can be established ‘for promoting commerce, art, science, religion, charity or any other useful object’, provided the profits, if any, or other income is applied for promoting only the objects of the company and no dividend is paid to its members\(^4\). The main instrument is a Memorandum and articles of association.

“A company may obtain nonprofit status if it fulfills the following conditions: the Memorandum of Association of the Company makes it expressly nonprofit; the income of the company is solely applied for promotion of charitable objectives; and the members do not get any dividends or other profits. Such companies are known as charitable companies and can hold property for charitable purposes. In such cases, this must be stated in the Memorandum of Association and the central government has to grant a license. The registration procedure for a company is elaborate and requires the submission of a printed Memorandum of Association and Articles of the Association to the Register of Companies”\(^5\).

Important features of section 25 company:
- It is a legal entity which can own its funds and other property.
- Less interference from government, more freedom in working as compared to trusts and societies.
- Better management and governance system than trusts and societies.
- An incorporated company has perpetual succession. Notwithstanding any changes in the members of the Company, the Company will be a same entity with the same privileges, immunities, estates and possessions. The Company shall continue to exist till its wound up in accordance with the provisions of the relevant law.
- It has to ensure that the profits are not distributed as dividend to its members and is used solely for the object of company.
- Any change in Memorandum of Association needs approval of Central Government
- The process of closing down a company is not easy as compared to trust and society. It involves compliance of various formalities.
### 3.3 COMPARISON AMONG TRUST, SOCIETY AND NON-PROFIT COMPANY

#### Table 3.1: Comparison among Trust, Society and Non-profit Company

<table>
<thead>
<tr>
<th>Differential factor</th>
<th>Trust</th>
<th>Society</th>
<th>Section-25 Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statute/Legislation</td>
<td>Relevant State Trust Act or Bombay Public Trusts Act, 1950</td>
<td>Societies Registration Act, 1860</td>
<td>Indian Companies Act, 1956</td>
</tr>
<tr>
<td>Jurisdiction</td>
<td>Deputy Registrar/Charity commissioner</td>
<td>Registrar of societies (charity commissioner in Maharashtra)</td>
<td>Registrar of companies</td>
</tr>
<tr>
<td>Registration</td>
<td>As trust</td>
<td>As Society In Maharashtra, both as a society and as a trust</td>
<td>As a company u/s 25 of the Indian Companies Act.</td>
</tr>
<tr>
<td>Registration Document</td>
<td>Trust deed</td>
<td>Memorandum of association and rules and regulations</td>
<td>Memorandum and articles of association and regulations</td>
</tr>
<tr>
<td>Stamp Duty</td>
<td>Trust deed to be executed on non-judicial stamp paper, vary from state to state</td>
<td>No stamp paper required for memorandum of association and rules and regulations.</td>
<td>No stamp paper required for memorandum and articles of association.</td>
</tr>
<tr>
<td>Board of Management</td>
<td>Trustees / Board of Trustees</td>
<td>Governing body or council/managing or executive committee</td>
<td>Board of directors/Managing committee</td>
</tr>
</tbody>
</table>
3.4 INDIA’S TAX LAWS AFFECTING NGOs

3.4.1 Income of NGOs: NGOs are taxable on basis of their income. The income of an NGO may include:

i) Subscriptions from the members;
ii) Donations and voluntary contributions from the members and others, including the donations towards the corpus of the trust or institution;
iii) Income from property held under trust (including a business undertaking so held);
iv) Capital gain on transfer of property held under trust;
v) Income from any other business carried on by the organisation which is incidental to the attainments of its objectives;
v) Income from any other business carried on by the organisation.

3.4.2 Tax exemptions for NGOs

1. General scheme:

The Income Tax Act, 1961 is the national all-India Act which is applicable to NGOs. It governs tax exemption for NGOs. Organizations eligible for tax-exempt status if the following conditions are met:

- They must be organized for religious or charitable purposes;
- The organization must spend 85% of its income on the objects of the organization;
- The organization must use funds for benefit of the public and not for the founder or trustee;
- Annual income return should be filed in time by the organization;
- The income should be applied in India
2. **Corpus donations:** Corpus donations are capital contribution and are not denoted as income. (It is invested and its interest/ dividend will be income).

3. **Business Income:** Under amendments to Section 11(4A) of the Income Tax Act 1961, a not-for-profit organization is not taxed on income from a business that it operates that is incidental to the attainment of the objects of the not-for-profit organization, provided the entity maintains separate books and accounts with respect to the business. Furthermore, certain activities resulting in profit, such as renting out auditoriums, are not treated as income from a business.

4. **Disqualification from Exemption:** Following groups are ineligible for tax exemption: all private religious trusts; and charitable trusts or organizations created after April 1, 1962, and established for the benefit of any particular religious community or caste. But note that a trust or organization established for the benefit of "Scheduled Castes, backward classes, Scheduled Tribes or women and children" is an exception; such a trust or organization is not disqualified, and its income is exempt from taxation.

3.4.3 **Tax Deduction for Donors**

The Income Tax Act, section 80G, sets forth the types of donations that are tax-deductible. The Act permits donors to deduct contributions to trusts, societies and section 25 companies. Many institutions listed under 80G are government-related; donors are entitled to a 100% deduction for donations to some of these government funds. Donors are generally entitled to a 50% deduction for donations to non-governmental charities. Total deductions taken may not exceed 10% of the donor's total gross income.

In – kind donations are not tax-deductible under Section 80G. Under section 35AC of the Act, donors may deduct 100% of contributions to various projects, including: 1) construction and maintenance of drinking water projects in rural areas and in urban slums; 2) construction of dwelling units for the economically disadvantaged;
and 3) construction of school buildings, primarily for economically disadvantaged children.

Under section 35CCA of the Act, donors may deduct 100% of their contributions to associations and institutions carrying out rural development programs and, under Section 35CCB of the Act, 100% of their donations to associations and institutions carrying out programs of conservation of natural resources.

A weighted deduction of 125% is also allowed for contributions to organizations approved under section 35(1)(ii) (a scientific research institute or a university, college or other institution) specifically for "scientific research," and for contributions made under section 35(1)(iii) specifically for "research in social science or statistical research."

3.4.4 Foreign Contribution Regulation Act (FCRA)

“The Foreign Contribution (Regulation) Act, 2010 (42 of 2010) dated the 26th September, 2010 was notified in the Gazette of India – Extraordinary – Part II - Section I dated the 27th September, 2010. However, the Act has come into force with effect from the 1st May, 2011 vide Gazette Notification vide G.S.R. 349 (E) dated the 29th April, 2011. Consequently, the earlier Act, viz., the Foreign Contribution (Regulation) Act, 1976 has been repealed. The Foreign Contribution (Regulation) Rules, 2011 made under section 48 of FCRA, 2010 have also come into force simultaneously with FCRA, 2010 vide Gazette Notification vide G.S.R. 349 (E) dated the 29th April, 2011.”

FCRA 2010 is an improved version of FCRA 1976 and it contains stringent provisions to ensure there is no mis-utilization of the foreign contribution. “The prime objective of the Act is to regulate the acceptance and utilization of foreign contribution and foreign hospitality by persons and associations working in the important areas of national life.”

FCRA is regulated by the Ministry of Home Affairs, Government of India. Every certificate of registration granted under FCRA, 2010 is valid for a period of five years from the date of its issue and then it has to be renewed. The renewal process is faster than the registration process.
3.4.5 Double Tax Treaty\textsuperscript{13}:
India and the United States signed a double-tax treaty on September 12, 1989. The treaty does not address issues related to charitable giving or not-for-profit entities.

3.5 REGULATORY FRAMEWORK

There are so many regulations on NGOs. Charitable trusts registered under the Bombay Public Trusts Act 1950, applicable in Gujarat and Maharashtra, are regulated by the Charity Commissioner in respective states. Societies registered under Societies Registration Act 1860 are regulated by the Registrar of Societies and in Maharashtra state by Charity Commissioner. Section 25 company registered under Indian Companies Act 1956 are regulated by the Registrar of Companies.

**Reporting requirements:**
Trusts have to file annual reports and audited accounts. Societies have to submit annual report and list containing details of managing body every year to Charity Commissioner of that state. A section 25 company has to file an annual report, audited accounts an annual return and main resolutions to the Registrar of Company. All the rules and regulations laid down in the respective Acts have to be followed by all the organizations.
3.6 OBSERVATIONS – “COMPLEXITIES IN THE LEGISLATION”

To understand the complexities in the legislation, interviews of some knowledgeable persons and experts related with the NGO sector were conducted (Annexure: 7 to 13). Also a case study was done for the same purpose (Annexure: 15). The observations from these interviews and case study yielded following conclusions:

- Bombay Public Trusts Act 1950 and Societies Registration Act 1860 are age old Acts. These acts are not amended since their date of inception. They should be modified to suit the present time or development changes.

- The case study (Annexure 15), reveals the inconvenience faced by a trust in the “process of change of name of the trust”. This case also talks about the time factor and inadequacies of the Bombay Public Trusts Act 1950.

- Registration process of trusts and societies, takes longer time due to inadequacy of staff at the Joint Charity Commissioner’s department.

- There are total 52277 trusts in Pune district as on 19.12.13. NGOs are increasing day by day. It is difficult to control population of NGOs (Annexure 12).

- About 10 % to 20 % NGOs are prompt in reporting to the Charity Commissioner. (Annexure 7, 8 and12).

- Findings for years 2009 to 2012, shows that approx. 71% of Section 25 companies, have reported in time to ROC (balance sheets and annual reports) (Annexure 11).

- Experts (Charity administration authorities, lawyers, Chartered Accountants, Company secretaries, authorities of Registrar of Companies) agree that there is need of such a platform where there will be interactions between Charity administration authorities, lawyers, Chartered Accountants, Company secretaries, authorities of Registrar of Companies and NGOs to understand the gaps in
existing systems. Only, if authority and power is assigned to this platform necessary amendments could be done. (Annexure : 8, 9, 12)

- Companies Act 1956 will now be replaced in year 2014 by Companies Act 2013. Companies Act 2013 is more wider than Companies Act 1956 and also there is much clarity. (Annexure 9,10)

- In proposed Companies Act 2013, company will have to spend 2% (minimum) of the average net profits on CSR. If in any case company cannot spend such amount, it should be reported with reasoning for not doing so. Due to this rule, the total CSR percentage will increase definitely (Annexure 11).
SUMMARY:

NGOs are entities with legal existence. NGOs are registered under different enactments depending upon the purpose of its formation. NGOs have regulatory framework of different acts. NGOs face many complications in laws related with NGO.

It is observed that many NGOs are not prompt in following the rules and regulations given under the enactments. The number of NGOs is increasing but it is difficult to control the growth due to ineffective system. Lack of manpower at Charity Commissioner’s department (Pune) is a constraint.
References:

1. http://ngosindia.com/resources/ngo_registration.php (web portal for NGOs in India)
3. Ibid 1
4. Ibid 1
5. Siddhartha Sen (Morgan State University Baltimore, Maryland, USA), Defining the Nonprofit sector: India, 1993, Working Papers of the The Johns Hopkins Comparative Nonprofit Sector Project Lester M. Salamon, Director Helmut K. Anheier, Assistant Director, USA, Page 22
6. Ibid 1
8. Ibid 1
9. Ibid 1
10. Ibid 1
12. Ibid
13. Ibid 1