

# *Non-Profit Organizations (NPOs)*

*Guest Speaker session by :*

*Ms. Taha Khan Baqai – FCA  
Director Tax Legal Services*

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# *Topics covered*

1. Brief Background facts and role of NPOs in Pakistan
2. Definition of NPOs under the Income Tax Ordinance, 2001
3. Important provisions of the Ordinance for NPOs
  - 3.1 Section 100C tax credit regime
    - 3.1.1 Persons eligible for 100C Tax regime
    - 3.1.2 Incomes qualified for 100C tax regime
    - 3.1.3 Conditions for claiming 100C tax regime
      - 3.1.3.1 Capping of administrative and management expenses
      - 3.1.3.2 Approval of the Commissioner
      - 3.1.3.3 Meaning of “Private benefit”
      - 3.1.3.4 Filing of statement of donations and voluntary contributions
  - 3.1.4 Surplus Funds

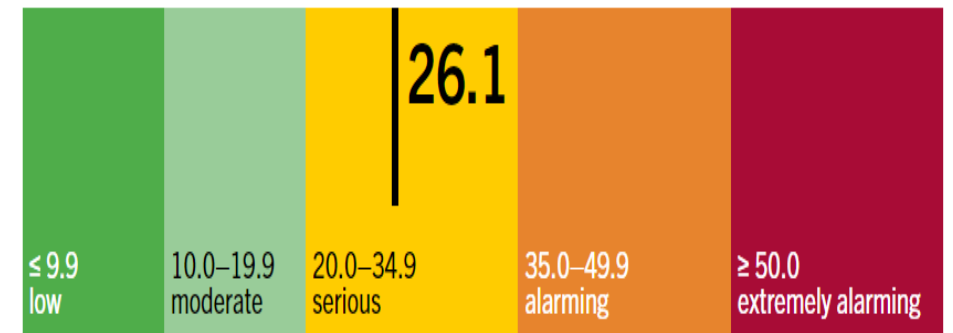
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## *Topics covered – continued...*

- 4. Practical issues related to tax credit u/s 100C / Relevant judgements
  - 4.1 Approval of Commissioner u/s 100C(1)(e) read with 2(36)(c)
  - 4.2 Approval of Chief Commissioner u/s 100C(2)(c)
  - 4.3 Validity of approval u/s 2(36)(c)
  - 4.4 Pendency of approval u/s 2(36)(c)
  - 4.5 Surplus Funds
  - 4.6 International NGOs / NPOs, being non-resident, not subject to tax on Pakistan for Foreign source income
  - 4.7 Obtaining exemption certificates from the Commissioner for non-withholding of income tax

# 1. *Brief background facts and role of NPOs in Pakistan*

- Pakistan ranks 99th among 121 countries according to 2022 Global Hunger Index with a score of **26.1**. Per that index, Pakistan has a level of hunger that is **serious**.
- 52% of Pakistan's population is facing multidimensional poverty (health, education and standard of living).
- 30% of population is dealing with food insecurity .
- 44% of minor population is not attending school.



# ***1. Brief background facts and role of NPOs in Pakistan continued .....***

- In this context, the role of non-profit organizations (NPOs) is crucial for elevating the socio-economic status of people.
- Various NPOs are working across the country to alleviate poverty and to improve social welfare.



# ***1. Brief background facts and role of NPOs in Pakistan continued .....***

- work for social welfare, socio-economic development, public health, education and poverty alleviation on a non-profit basis.



## 2. *Definition of NPOs under the Ordinance*

### Section 2(36) of the Income Tax Ordinance, 2001

- person other than an individual.
- established for religious, educational, charitable, welfare purposes for general public\* or for the promotion of an amateur sport.
- formed and registered by or under any law as a non-profit organization (The Societies Registration Act, 1860, The Trusts Act, 1882, the Companies Act, 2017, The Co-operative Societies Act, 1925, Trade Organisations Ordinance, 2007, Non-Profit Public Benefit Organisations (Governance and Support) Act, 2003, Mussalman Waqf Act, 1923, Charitable Endowments Act, 1923 etc).
- approved by the Commissioner as an NPO (procedure prescribed in Rules 211 to 217).

**Condition:** none of the assets of such person confers or may confer a private benefit to any other person.

*\* Added via Finance Act, 2020*

### 3. Important provisions of the Ordinance for NPOs

#### **Before Finance Act, 2014**

- Blanket tax exemption for persons and incomes under clauses;
  - (58),
  - (58A)
  - (59) and
  - (60)

#### **After Finance Act, 2014**

- Introduction of 100% Tax credit regime u/s 100C on tax payable including minimum tax, final tax.
- ACT is not applicable.
- Any income of persons under Table I of clause (66) of Part I of Second Schedule to the Ordinance is still exempt from tax.



## 3.1 Section 100C – Tax credit regime

Persons

Incomes

Conditions

Surplus  
funds

### 3.1.1 Persons eligible for 100C Tax regime

1. Persons specified in Table II of clause (66) of Part I of Second Schedule;
2. Trusts under the scheme approved by the GoP;
3. Trusts [defined in section 80(2)(d)];
4. Welfare Institutions registered under laws related to social welfare department;
5. Not for profit organizations registered with SECP u/s 42 of the Companies Act, 2017;
6. Welfare societies registered under laws related to co-operative societies;
7. Waqf registered under Mussalman Waqf Validating Act, 1913;
8. University or education institutions run by NPOs;
9. Religious or charitable institutions;
10. International non-governmental organizations (INGOs).

**For S No. 2, 3, 4, 5, 8, 9, tax exemption was provided in clause (58), (58A), (59) and (60) but in 2014, these were brought in section 100C as tax credit**

**S No. 1, 6, 7, 10 introduced vide FA 2021**

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### 3.1.2 Incomes qualified for 100C tax regime

1. Donations, voluntary contributions and subscriptions;
2. Income from house property;
3. Investments income on Federal Government securities;
4. Profit on debt from scheduled banks and microfinance banks;
5. Government grants;
6. Income from business as is expended in Pakistan for the purposes of carrying out welfare activities\*;
7. Any income of the persons in Serial nos. 1, 2 and 8 as mentioned in previous slide;

*\* Proportionate income will be eligible for tax credit.*

### 3.1.3 Conditions for claiming 100C tax regime

- a. Filing of Annual tax Return;
- b. Withholding and collection of tax duly made and deposited;
- c. Filing of Withholding tax statements;
- d. Capping of administrative and management expenditures upto 15% of total receipts  
(Further discussed in subsequent slides);

**Exception: NPOs** have commenced charitable and welfare activities for the first time within last 3 years OR total receipts are less than Rs. 100 million.

**Inserted vide  
FA 2017**

### 3.1.3 Conditions for claiming 100C tax regime - *Continued.....*

- e. Approval of Commissioner u/s 2(36) (Further discussed in subsequent slides);  
**Exception:** Persons in Table II of clause (66) are required to obtain approval from July 1, 2023 and the said requirement has been waived for prior years.
- f. No private benefit from the assets of Trust or welfare institutions (Further discussed in subsequent slides);  
However, if private benefit conferred, such amount of benefit is added to income of the donor.
- g. Filing of Statement of voluntary contributions and donations received in immediately preceding tax years. (Further discussed in subsequent slides)

### **3.1.3.1 Capping of administrative and management expenses**

1. Definition of 'administrative and management expenses' is not given under the Ordinance;
2. Operational / Project expenses of NPOs are not covered under Administrative and Management expenses [Circular 4 of 2017 dated September 6, 2017];
3. Rationale behind the said insertion in the law is to stop misuse of receipts / donations etc. received by NPOs and discourage them from spending such amounts on huge administrative salaries, vehicles etc; [Circular 4 of 2017 dated September 6, 2017];
4. Per Circular 4 of 2017 dated September 6, 2017, the limit for Administrative and Management expenses is applicable to NPOs only and not to trusts and welfare institutions. The examples given in the circular also relate to NPOs.
5. In our view, disqualification of 100% tax credit upon exceeding the limit of 15% of certain expenses is harsh. Instead of disallowing the tax credit, the excess expenditure could have been subjected to tax.

### 3.1.3.1 Capping of administrative and management expenses – *continued .....*

6. The examples of various expenses given in the abovementioned circular are as under:

#### **Administrative and Management expenses**

- Salaries of Administrative Officers and staff
- Rent of office
- Vehicle running expenses
- Utilities

#### **Project expenses**

- Salaries of teachers / school staff
- Rent of School buildings
- Books and stationery
- Utilities
- Transportation

### 3.1.3.2 Approval of the Commissioner

- **Rule 211** - Procedure for the approval of NPOs u/s 2(36)(c), following documents alongwith application (prescribed format), to be submitted:
  - Constitution documents (Memorandum and Articles of Association, Trust deed, Certificate of incorporation etc.), certificate of registration etc.
  - Details of the members / Trustees / promoters.
  - Performance Evaluation Report for preceding financial year, duly approved by Independent Certification Agencies (Pakistan Centre of Philanthropy). The applicant can get the Performance report appraised by CCIR, RTO or LTO, till the time two certification agencies are approved by the FBR / GoP.
  - Financial Statements; etc.
- **Rule 213** – Refusal to grant approval by the Commissioner if the NPO:
  - is being used for personal / private benefit in the form of dividend, bonus etc.
  - the constitution documents do not restrict surplus or monies (excluding restricted funds) upto 25% of Total income.
  - Constitution documents do not provide for transfer of assets to another NPO on its dissolution.
  - Not being able to achieve the aims and objectives of NPOs



## 3.1.3.2 Approval of the Commissioner

*Continued ....*

- the salary expense exceeds the prescribed capping of 50% of total receipts excluding restricted donations or funds.

*[Circular no. 2 of 1996: The real test to be applied in such cases is to see that the institution has been established solely for educational purposes and not for purposes of profit. In order to ascertain that, it has to be seen that the profits or surplus of the educational institution is not diverted to the personal benefit of the proprietor, sponsor, partner or the directors of the educational institutions.]*

- **Rule 214** – Validity of approval for 3 years unless withdrawn earlier.
- **Rule 215** – The CIR is required to finalise the NPO approval application within two months of receipt.
- **Rule 217** – Power to withdraw approval, however, prior opportunity of being heard to be provided to the NPO.
- **Rule 220** – Commissioner has powers to relax the requirements and conditions under the Rules.

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### 3.1.3.3 Meaning of “Private benefit”

1. Private benefit means **any benefit** from the assets of the Trust and Welfare institution conferred by the Donors, family, children, author of the trust or descendants or the maker of the institution or any other person. [Section 100C(4)(f)].
2. The amount of such benefits shall be added to the income of the donor of the Trusts / Welfare Institution. NPO is not mentioned in Section 100C(4)(f).

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### **3.1.3.4 Filing of statement of donations and voluntary contributions**

1. This condition was present in Rule 217 since 2006, but was applicable for NPOs only.
2. Through the FA 2020, this condition has been added to Section 100C(4)(g) and is now applicable to all entities falling under 100C.
3. The statement should show the names and addresses of the persons from whom donations, contributions, subscriptions etc. exceeding Rs 5,000 received during the tax year.

## 3.1.4 Surplus funds

**Surplus funds of organisations (to which 100C applies) are taxable @ 10%.**

Surplus funds mean funds or monies:

- a) not spent on charitable and welfare activities during the tax year;
- b) received during the tax year as donations, voluntary contributions, subscriptions and other incomes;
- c) which are more than 25% of the total receipts of the NPO received during the tax year; and
- d) are not part of the restricted funds\*.

*\* Restricted funds mean any fund received by the organization but could not be spent and treated as revenue due to any **obligation placed by the donor**.*

## **4. Practical issues related to tax credit u/s 100C / Relevant judgements**

1. Approval of Commissioner u/s 100C(1)(e) read with section 2(36)
2. Approval of Chief Commissioner u/s 100C(2)(c)
3. Validity of approval u/s 2(36)(c)
4. Pendency of approval u/s 2(36)(c)
5. Surplus funds
6. International NGOs / NPOs, being non-resident, not subject to tax in Pakistan for Foreign source income
7. Obtaining exemption certificates from the Commissioner for non-withholding of income tax

## 4.1 Approval of Commissioner u/s 100C(1)(e) read with 2(36)(c)

### Background of the Provision

- From July 2020, approval from Commissioner u/s 2(36)(c) is required for entities claiming tax credit u/s 100C. Since NPOs by their very definition were required to obtain NPO approval, this requirement was applicable to Trusts and Welfare organisations, etc. from this date.

**Exception:** Persons under Table II of clause (66) of Part I are required to obtain approval w.e.f July 1, 2023 and waiver has been granted for prior years.

## 4.1 Approval of Commissioner u/s 100C(1)(e) read with 2(36)(c) – *continued .....*

### Relevant Judgements

- Appellate Tribunal Inland Revenue, Lahore decision bearing ITA no. 1429/LB/2020 dated October 2, 2020 in case of M/s Fatima Fertilizer Welfare Fund, Mukhtar Garh, Bahalwarpur (FFWF)
  - Being a welfare institution, FFWF claimed 100% tax credit for tax year 2016. The claim was rejected on the basis on non-approval of Commissioner u/s 2(36)(c).
  - The ATIR held that the said requirement for welfare institutions is applicable from July 1, 2020, and it was not required for impugned tax year. Therefore, tax credit u/s 100C was allowed.

## 4.1 Approval of Commissioner u/s 100C(1)(e) read with 2(36)(c) – *continued .....*

### **Other Judgements**

- **Appellate Tribunal Inland Revenue, Islamabad decision bearing ITA no. 748/IB/2021 dated January 10, 2022 in case of National Support Rural Program. [Requirement for approval u/s 2(36) not applicable prior to July 1, 2022, for persons listed in Table II of Part I, 2<sup>nd</sup> Sch]**



## 4.2 Approval of Chief Commissioner u/s 100C(2)(c)

### Background of the Provision

- Approval from Chief Commissioner u/s 100C(2)(c) required for Trusts, welfare institutions and non-profit organizations. [inserted vide FA 2014 and omitted vide FA 2019, hence it was part of the law for TY 2015 to 2019].
- The form and procedure is prescribed in Rule 220A of the Rules. The process is similar to that of seeking NPO approval from the Commissioner.
- **Controversy** - Such approval is not required if a person qualified for 100% tax credit under any other clause other than section 100C(2)(c). For example, a University being run by NPOs for educational purposes and not for profit.

## 4.2 Approval of Chief Commissioner u/s 100C(2)(c) *continued .....*

### **Relevant Judgements**

- **Islamabad High Court decision bearing reference no. I.T.R No. 94 of 2022 dated September 29, 2022 in case of Al-Mizan Foundation (AMF)**
  - Petitioner is a Charitable Trust registered under Societies Registration Act, 1860
  - Proceedings under section 122(5A) were conducted for tax year 2015
  - The Hon'ble IHC held that Trust falls under clause 100C(2)(c) is required to obtain CCIR approval for the impugned tax year for entitlement of 100% tax credit. Furthermore, the said clause was omitted vide FA 2019, hence, not required for subsequent periods and the tax credit was disallowed. The judgement is based on the assumption that redundancy cannot be attributed to the provisions of the law.

## 4.2 Approval of Chief Commissioner u/s 100C(2)(c) *continued .....*

**Judgements related thereto are:**

- **Appellate Tribunal Inland Revenue, Karachi decision reported as 2020 PTD 1583 dated May 6, 2019 in case of M/s Messrs. Ziauddin University, Karachi**
  - The Appellant is a University, which is holding status of NPO u/s 2(36)(c), claimed tax credit u/s 100C. The tax officer held that approval from the CCIR is required in section 100C(2)(c).
  - It was argued that the said approval was not required as the appellant falls under clause 100C(2)(d).
  - The ATIR however, remanded back the case for re-examination. However, it was, in principle, held that approval from CCIR would be required in order to claim tax credit u/s 100C.

**ISSUE UNRESOLVED – Since the condition is not mentioned as a pre-requisite for availing 100% credit, the same should not be made basis for rejection of the said credit.**

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## 4.3 Validity of approval u/s 2(36)(c)

- As per Rule 214, the approval granted by the Commissioner u/s 2(36)(c) is valid for subsequent 3 years unless withdrawn.
- Practically, FBR's Iris portal grants approval for 1 year only, requiring NPOs to apply the approval every year unnecessarily due to procedural / systematic limitations despite having it for 3 years.
- **Recommendation :** FBR to make necessary amendment on the FBR portal to avoid unnecessary complications.

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## 4.4 Pendency of approval u/s 2(36)(c)

- If an NPO applied for approval of Commissioner u/s 2(36)(c) but it is pending at Commissioner's part. The question here is whether or not the NPO / Welfare organization can file its return of income while claiming tax credit u/s 100C?

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## 4.5 Surplus funds

- Prior to FA 2017, if NPO does not spend more than 75% of its income for welfare/charitable activities, then the NPO would not be entitled to NPO approval and hence subject to tax at corporate rate of tax.
- To remove this harsh implication, concept of taxing surplus funds was introduced in 100C(5).
- Rule 213 in respect of the above has not been amended accordingly and still provide for the abovementioned condition.
- In our view, taxing surplus funds is not appropriate under the Strict Principles of Taxation as donations, voluntary contributions can not be considered as Income even if they are unspent as the same reflects a timing difference in expenditure pattern.

## 4.6 International NGOs / NPOs, being non-resident, not subject to tax on Pakistan for Foreign source income

- Concept separated from NGOs / NPOs vide FA 2021 by introducing a separate category.
- Foreign source income (i.e. grants, donations) are not subject to tax in Pakistan, not PSI.
- **Relevant Judgement**
  - Appellate Tribunal Inland Revenue, Islamabad bearing ITA No. 1055/IB/2021, 1056/IB/2021, 1057/IB/2021 dated February 23, 2022 in case of M/s Helpage International
    - Tax years involved 2015, 2016, 2017
    - Condition for obtaining NPO approval is applicable from TY 2019 for Trusts and Welfare institutions
    - Minimum tax u/s 113 is not applicable on non-resident persons
    - Foreign grants do not fall under the definition of 'turnover' in terms of section 113
    - Foreign grants are not even taxable in Pakistan being FSI

## **4.7 Obtaining exemption certificates from the Commissioner for non-withholding of income tax**

- Exemption certificate u/s 159 read with relevant sections of withholding of tax is required to obtain in order to avoid unnecessary blockage of funds
- Exception: Persons of Table I of Clause (66) of Part I of Second Schedule are not subject to withholding and collection of tax under clause (120) of Part IV of Second Schedule to the Ordinance. Practically, Exemption Certificates are obtained because of SHC judgement 2016 PTD 1204.
- Practical issue: Issuance of exemption certificates is delayed due to the condition of submission of Approval u/s 2(36)(c).
- Suggestion: Considering the precedence / past history, conditional exemption can be considered to be provided to NPOs, Welfare Organizations, Trusts, etc.



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*THANK YOU*

QUESTIONS  
AND  
ANSWERS