

# Paying for your sins - why enforcing tax laws on churches could be problematic

The case of self-proclaimed prophet Shepherd Bushiri and his wife, who were arrested by the Hawks earlier this year on charges of fraud and money laundering, has cast the spotlight on tax laws relating to churches and religious institutions, and whether any loopholes that exist are being exploited.



© serezhnyy – [123RF.com](https://www.123RF.com)

Cases like this have prompted the South African Revenue Service (Sars) to launch an investigation into religious institutions that are non-compliant with the country's tax law.

Louis Botha, an associate in Cliffe Dekker Hofmeyr's (CDH's) Tax and Exchange Control practice, says that while there is nothing wrong with the legislation that governs how churches and other religious institutions are taxed, enforcement of the law is where the challenge arises.

## Public Benefit Organisations

"Churches and religious institutions are not automatically exempt from paying taxes, as many people seem to think. If they seek tax exemption, these institutions need to apply to Sars to be approved as Public Benefit Organisations (PBOs)," says Botha.

According to Sars, an organisation will only enjoy preferential tax treatment after it has applied for and been granted approval as a PBO by the Sars Tax Exemption Unit, if it meets the requirements set out in the Income Tax Act, 1962.

“This means that they must show that they conduct public benefit activities related to their religion or belief. These activities must be carried out on a philanthropic basis – not for profit – and must be for the benefit of or accessible to the general public.”

Botha explains that tax-exempt religious institutions must be able to prove that their sole or main objective is to perform religious public benefit activities. They may also pay their employees remuneration that is not excessive having regard to certain factors, including what is generally considered reasonable in the sector. Employees are not exempt from paying tax on the remuneration received.

## **Tax-exempt activities**

“However, being approved as a PBO is not a way to avoid paying taxes. Once an institution is approved as a PBO, it may receive tithes or donations that are exempt from taxation and these may be used for religious public benefit activities. If the institution’s founding document makes provision for it to carry out other public benefit activities listed in the Income Tax Act, such as activities of a welfare and humanitarian nature, it may also use tithes or donations received for this purpose,” he says.

Should a religious institution use tithes or donations to carry out activities other than public benefit activities listed in its founding document, it will fall foul of the country’s tax laws.

## **Tax returns still mandatory**

Botha adds that even religious institutions that are registered as PBOs must submit annual tax returns and can be audited by Sars’ Tax Exemption Unit to ensure that they comply. This is an oversight mechanism to ensure that the system is not exploited by organisations that seek to avoid paying taxes.

Those institutions that conduct business activities, are used by their religious leaders for self-enrichment, or pay their employees “excessive” salaries, risk losing their PBO status.

## **Exceptions to exemption**

Even those institutions that are registered as PBOs do not have a blanket tax exemption and may have to pay income tax on their trading or business activities that fall outside the exemption stipulations. For example, if a church earns rental income from renting its premises to the public on a regular basis, such rental income will likely be taxable.

Botha explains that while the law is adequate and that legally no loopholes exist, the problem is with enforcing the legislation, as the Tax Exemption Unit appears to be substantially under-resourced.

“There is nothing wrong with the legislation. The issue is with enforcement. In practice it generally takes at least six months to get PBO status, from the date of submission of an application, so it is a comprehensive and rigorous process,” he says.

## **Clamping down**

Earlier this year, Sars announced that it will be investigating religious institutions that do not pay tax and warned that those that do not have tax-exempt status will be taxed like normal companies.

The investigation was sparked by a Sars study conducted a year ago that revealed how a number of other religious

institutions are incorrectly declaring their income tax.

Sars did not reveal the number of churches and other religious institutions that are exploiting the system and Botha says it is difficult to gauge how widespread the problem is. "It is not clear how many are not tax-compliant, but I imagine that there is a substantial number that needs to be investigated to determine the extent of the problem," he concluded.

For more, visit: <https://www.bizcommunity.com>