

Tax Exempt Organization and its Tax Exemption Certificates

According to sec.2 (dha) of Income Tax Act, 2058, the following organizations are the tax exempt organizations:

1. One of the following two organizations registered with the Inland Revenue Department as a Tax Exempt Organization:

- A social, religious, educational or **benevolent organization** of public nature established without any objective of generation of profit.
- An amateur sporting association established for the purpose to promote social or sporting amenities without having an aim to distribute the income among its members.

2. A **political party** registered with the Election Commission.

Provided that, the exempt organization's income is taxable in case the organization provides benefits to any person from its assets or income except in cases when the same is provided while completing the work as per the objective of organization or as a consideration for any assets or service received.

*. Here, **benevolent organization** is just like a social or charitable organizations established in Nepal pursuant to Social Registration Act, 2034 as a non- profit organization. It can also be incorporated as company not distributing profit under prevailing company law.

*. A political party registered with Election Commission does not require the tax exemption certificate from IRD.As the tax exemption certificate is utmost for all the tax exempt organizations registered for getting the exemption from taxes.

How to obtain the Tax Exemption Certificates

Rule 3 of Income Tax Rules describes regarding the registration of organization as a tax exempt organization. As per the rule, any organization entitled to enjoy tax exemption shall submit an application, accompanied by the following details, to the department for exemption of tax:

- A copy of registration certificate in case an organization is required to be registered pursuant to the prevailing law.
- A copy of statute of the organization which means by laws/MOA/AOA/Bidhan of the organization.
- A copy of Permanent Account Number Certificate
- A copy of audited financial statements, if applicable.

Upon conducting necessary examination as to the application submitted for tax exemption as above, IRD shall register such organization as an organization entitled to enjoy tax exemption and issue a certificate.

Further, IRD may prescribe certain organizations as TEO without requiring registration.

Moreover, Income Tax Manual, 2066 (Updated 2073) also requires the following conditions to be attached in Tax Exemption Certificate:

- TEO shall submit audited financial statements of the organization of each year within three months of the end of fiscal year.

- TEO shall withhold tax on payments attracting withholding tax and submit the returns and amount in respective tax offices.
- The person making payment of rent, interest, service fee, royalty or contract payments or gain on disposal of securities shall withhold tax as per the relevant provisions of the act. In case it appears that such amounts are not taxable, the same can be refunded from respective Inland Revenue Office.
- The auditor's report of TEO shall include the report as to whether the withholding taxes are deducted by TEO and whether the work of TEO is as per the objectives prescribed by the by- laws of TEO.
- TEO shall not conduct any activities beyond the scope of its objective prescribed through its registration document. Any amount received with respect to the activities conducted beyond the ambit of its object clause, it is taxable.

Renewal of Tax Exemption Certificate

The Income Tax Rules has made an amendment and added Rule 5A. The added provision requires the tax exempt entities to get their tax exemption certificate renewed with the Inland Revenue Department on an annual basis. The tax exempt certificate must be renewed within 3 months from the end of the fiscal year in practice. But, as per Rule 5A, the exemption certificate must be renewed within 6 months from the end of the fiscal year.

For renewal of the Exemption Certificates, the exempt organization shall file an application in the format prescribed by IRD along with the following documents:

- Proof of Filing of annual income returns.
- Proof of submission of withholding tax returns in relation to all withholding taxes.
- Proof of payment of withholding taxes in relation to tax withheld during the year.

It is also to be noted that if an exempt organization fails to renew its exemption certificates within the prescribed time period, the exemption certificate cannot be renewed. (IRD circular dated 2073/08/03).

Now a days, it has led to a confusion to the INGOs/NGOs with respect to the surplus amount taxed by the tax authorities though donation is exempt from tax. Because the existing tax return form (Schedule 5 of D 03 form) does not have a clear provision to include any grants income and related expenditure.

Some have submitted zero return, while others have submitted it showing equal amount of income and expenditure and have not been taxed thereon. Hence it is always better to show the income equal to expenses and file the return according to it.

Few of the points written above are the personal opinion which may defer in practice.

Thank you!