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PBO? NPC? NPO? – Unravelling the confusion

PBO – Public Benefit Organisation

Registration with SARS

NPC – Non-profit Company

Registration with CIPC

NPO – Non-profit Organisation

Registration with Department of Social Welfare (not compulsory)

An organisation that is established for a purpose other than to make a profit should be created under one of the following forms:

- Non-profit company
- Association
- Trust

The form that the organisation takes does not determine its tax status.

Every organisation so formed must register with SARS in order to be classified as TAX EXEMPT.

A step-by-step process:

1. Decide on what the purpose of the organisation will be.
2. Decide who will be the founding members – at least 3 unrelated people.
3. Decide on a name.
4. Decide on the form of the organisation.
5. Form the relevant organisation.
    a. Register an NPC with a MOI (Memorandum of Incorporation)
    or
    b. Form an Association with a Constitution
    or
    c. Register a Trust Deed at the Master's Office
6. Use the registered documents to open a bank account.
7. Apply to SARS for a PBO number.

The exemption provision

Section 10(1)(cN) of the Income Tax Act No. 58 of 1962 (the Act) exempts from income tax, receipts and accruals of any PBO approved by the Commissioner in terms of section 30(3) of the Act. Section 10(1)(cN) of the Act contains detailed rules governing the trading activities conducted by PBOs which will be dealt with below.

What constitutes a PBO?

Section 30(3) of the Act prescribes that the Commissioner shall approve a PBO which complies with various requirements. It is therefore important to establish what constitutes a PBO for the purposes of section 30 of the Act.

Thus, when creating a PBO a decision must be made whether to incorporate a company, register a trust or form an association of persons by way of a constitution.

- The Act requires that the PBO conducts its activities in a non-profit manner and with an altruistic or philanthropic intent.
- Furthermore, the activities conducted by the PBO cannot directly or indirectly enhance the economic self-interest of any person acting in a fiduciary capacity for the PBO or for an employee thereof, except in the form of reasonable remuneration payable to that fiduciary or employee for services rendered.
- In addition, at least 85% of the activities conducted by the PBO, measured either as the cost related to the activities or the time expended relating thereto must be carried out for the benefit of persons in the country.
- The definition requires that the PBO conducts its activities for the benefit of or is widely accessible to the general public at large, including any sector thereof.
- To qualify for recognition as a PBO the organisation must conduct a public benefit activity which is defined as any activity listed in Part 1 of the Ninth Schedule of the Act. Part 1 of the Ninth Schedule of the Act comprises eleven main categories of activities with the particular types of activities listed in each category. Currently the main categories are as follows:

    - welfare and humanitarian;
    - healthcare;
    - land and housing;

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- education and development;
- religion, belief or philosophy;
- cultural;
- conservation, environment and animal welfare;
- research and consumer rights;
- sport;
- providing of funds, assets or other resources;
- general.

The requirements contained in section 30(3) of the Act

A PBO wishing to secure recognition by the Commissioner: SARS must comply with the requirements contained in section 30(3) of the Act which are considered below.

When the PBO applies for exemption it must submit to the Commissioner a copy of its constitution, will or other written instrument under which it was created.

The Act requires that the PBO must have **at least 3 persons, who are not connected persons in relation to each other to accept fiduciary responsibility of the PBO**. Furthermore, **no single person can directly or indirectly control the decision making powers of the PBO.**

Furthermore, the PBO must be prohibited from distributing any of its funds to any person, otherwise than in the course of undertaking its activities. The PBO must use its funds solely for the object for which it has been established and is required to invest its funds with either a financial institution as defined in section 1 of the Financial Services Board Act No. 97 of 1990, or in any South African listed shares or in such other prudent investments in financial instruments and assets as the Commissioner may determine after consultation with the executive officer of the Financial Services Board and the director of non-profit organisations. Where the PBO acquired, for example, unlisted shares by way of donation, bequest or inheritance it is entitled to retain that investment. However, a PBO is prohibited, under the current provisions, from acquiring shares in unlisted companies or making other investments besides those listed above.

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If the PBO is dissolved it **must transfer its assets to a similar PBO which has been approved in terms of section 30 of the Act** or to any other institution, board or body which is exempt from tax under the provisions of section 10(1)(cA)(i) of the Act, which has as its sole or principal object the carrying on of any public benefit activity or to any department of state or administration in the national, provincial or local sphere of government in South Africa.

In addition, the PBO **cannot accept donations which are revocable at the instance of the dono**r for reasons other than the material failure to conform to the designated purposes and conditions of such donation..

If the PBO wishes to amend its founding document it must submit a copy of the proposed amendments to the Commissioner for approval.

The rules governing the investment of funds, dissolution of the PBO, nature of persons acting for the PBO and amendment of the PBO' s founding document must be set out in the PBO' s articles, deed or constitution.

Other requirements

A PBO enjoys a privileged position in that it is not subject to tax on the income derived by it. Thus the PBO **must comply with the requirements for exemption** on an ongoing basis and in addition comply with other requirements contained in section 30(3) of the Act.

Further, the PBO must **not pay remuneration which is excessive** when reference is made to what is generally considered fair remuneration in the particular sector and in relation to the services rendered by the PBO' s office bearers.

In addition, the PBO **must comply with such reporting requirements** as may be determined by the Commissioner. The PBO, once approved by the Commissioner, must submit an annual tax return together with supporting annual financial statements so that the Commissioner can ensure that the PBO has conducted public benefit activities in the prescribed manner for the particular year.

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Books of account

Section 30 of the Act requires that the PBO must retain and preserve its books and records for a period of 4 years after the date of last entry in any book or where the records are not kept in book form, be retained and preserved by any person in control of such PBO for a period of 4 years after completion of the transactions, acts or operations to which they relate.

The trading rules

The Act now recognises the concept of partial exemption thereby allowing PBOs to retain, for example, rent producing properties without jeopardising the tax exempt status of the PBO itself. Section 10(1)(cN) of the Act refers to various categories of trading activity, each of which will be dealt with below.

Trading activities not subject to tax

If the trading, undertaking or activity is integral and directly related to the sole object of the PBO and is carried out and conducted on the basis substantially the whole of which is directed towards the recovery of cost and does not result in unfair competition in relation to taxable entities, the trading activity will not attract tax. Where, for example, a school charges school fees for the tuition of students, the income derived therefrom would be exempt under this category contained in section 10(1)(cN)(ii)(aa)(A) of the Act.

Where the PBO conducts the trading activity occasionally and substantially with assistance on a voluntary basis, the income derived by it will not be subject to tax. An example in this regard would be the church or synagogue that runs a fête selling items made available by congregants and the congregants volunteer their services to the organisation without receiving any payment therefor. Other examples include cake sales or raffle tickets sold by a PBO where the prizes have been donated to the PBO.

Permitted trading

Under section 10(1)(cN) of the Act where the income derived from trading does not exceed the greater of 5% of the total receipts and accruals of the PBO during the relevant year of assessment or R200 000, the trading income so derived will be exempt from income tax.

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Section 18A

Section 18A provides that a deduction (subject to a limit) is allowed in respect of the sum of donations in cash or in kind made by a taxpayer, during the year of assessment to an approved PBO.

To gain approval the PBO activities must be in line with Part II of the Ninth Schedule

- welfare and humanitarian
- health care
- education and development
- conservation, environment, and animal welfare
- land and housing

as broad categories.

Conclusion

It is apparent from the above that there are several hurdles that must be crossed before a PBO will be recognised by the Commissioner.

It would be advisable to discuss the future of you PBO with a professional who can assist you and ensure that your organisation is compliant as the burden of responsibility on directors is heavy.