

Zakāt on Non- Agricultural Land Plots: Public Awareness and Fiscal Reforms

• **Dr. Mohammad Farooq**

•• **Dr Naila Nazir**

Abstract:

Zakat is although a compulsory obligation in Islam but is not paid compulsorily by the people. There are two main reasons; one is the ignorance about many things on which zakat is due, for example non-agricultural land and commercial plots etc. and second, ignorance about the mechanism through which it is paid. The first aspect is related to public awareness and second aspect is related to the fiscal policy being enforced by the government collecting property and wealth taxes thus putting heavy financial pressure on the owners of real estate so as to compel them to avoid zakat and pay taxes. The paper explores the level of awareness among the general public about the payment of zakat on non-agricultural land. It further addresses the question that how the existing revenue structure need to be changed. For the first aspect, primary data with n=33 has been collected from the capital city of the province Khyber Pakhtunkhwa. For the second aspect the revenue structure of the government is reviewed to find out the number of taxes on the possession, sale and purchase of commercial or non-agricultural land plots. Since taxes are in no way a substitute of zakat so it is further explored that if the existing taxes are replaced and zakat system would be properly enforced then how much is the net return. In order to estimate this net return, an interview has been conducted from the property dealers and also the figures are taken from government accounts to calculate a sample for the study area that is then generalized for the government returns at large. The results of the study show a high level of ignorance about zakat obligation on plots in the study area. The verdicts of the Islamic scholars also create difference of opinion, however, majority have approved the case in favor of payment. Since there is ignorance and

• *Assistant Professor of Economics, Sheikh Zayed Islamic Centre, University of Peshawar, KP, Pakistan.*

•• *Assistant Professor of Economics, Department of Economics, University of Peshawar, KP, Pakistan.*

people have to pay taxes so they avoid zakat and just pay taxes. A mechanism is needed for fiscal reforms to ensure the payment of zakat and to stop its substitution against taxes on land plots.

Introduction:

Zakat and government fiscal policies in Pakistan are conducted separately. Pakistan started Islamization of the economy during 1980s and has a name in the list of those Islamic countries that work towards Shariah-based economic practices, but unfortunately Islamization of the economy is always misunderstood. All the efforts which are made in this way always directed towards Interest-Free Banking, whereas interest-free banking does not always mean Islamic Banking. Islamization of the economy means reforming all sectors of the economy; from monetary policy to fiscal, from consumption to production and from marketing to sales, all should be Shariah-compliant. Islamic economic principles are practiced partially. The Muslim countries like Pakistan are reforming only monetary sector, whereas fiscal sector is ignored. Since, there is a heavy burden of taxes on the general public so they avoid zakat or bother less about its proper payment. The opinion of the religious scholars also differ in this matter; some are of the view that from the value of the asset the taxes paid should be subtracted and then zakat should be paid on the remaining amount. Some are of the opinion that zakat is calculated from the total value of the asset. The government of Pakistan could easily develop a mechanism through which these problems can be solved. There is a fear, lack of confidence at national level and propaganda by the western economic managers that if taxes would be reduced or abolished then the government would be bankrupt and would have nothing to run the affairs of the country. The fact is that Islamic state has many sources of revenue, zakat is one among them. There are many areas within zakat head which are not known to or familiar to the general public for the obligation of zakat that could have lot of potential revenue. The present study is an attempt to explore such areas and addresses the question of reforming federal revenue system so as to remove the hurdles in the way of proper implementation of zakat system. One such area is payment of zakat on non-agricultural land commonly known as plots being held by individuals and families. Regarding this matter there are four situations; first, one person has bought a plot for the construction of his house; second, the person has bought more than one plot so as to sell all at the end to buy one house because houses are expensive and you can't buy one house by selling one plot; third, he has bought more than one plot on installment basis and none of the plot has yet come under his ownership and fourth, the plot(s) are entirely meant for trade purpose i.e. buying plot to sell when market is favorable. Awareness about zakat payment in all these cases is not there in the country. There are two reasons; one, people have no knowledge about the real

estate and its zakat obligation, second, they are bearing heavy burden of taxes so they just avoid zakat. In order to find out the solution the study designs the following objectives:

Objectives:

The objective of this research is to present a case of a Muslim country Pakistan where above 96% of the population is Muslim but lack awareness about the obligation of zakat for important assets like land plots. The study aims at considering the matter in the light of fiscal structure of the country. In this context, specific objectives are:

- To find out the level of awareness about zakat payment on non-agricultural plots in the study area.
- To review the opinion of the religious scholars about the obligation related to the matter and rate of Zakat payment on plots.
- To describe the number of taxes and rate of taxes on the possession and sale of plots.
- To consider the replacement of taxes to ensure the payment of zakat on land plots so as to make the zakat system more effective.

Hypothesis:

- The level of payment of zakat on non-agricultural plots in the study area is fifty percent.
- The tax rate on plots in the study area is below the rate of zakat.

Methodology:

In order to meet the objectives and to test the hypothesis the data for the study includes both primary and secondary. For primary data the capital city Peshawar of Khyber Pakhtunkhwa province is selected. In the capital city, people from all twenty four districts are settled. Sample size with $n = 33$ families is selected. An interview has been arranged with these families about the payment of zakat on plots they possess. These families have been selected on the basis of the possession of the assets particularly land plots. An effort has been made to select educated people. The information about their awareness, payment of zakat and method of payment has been collected. The reasons of non-payment are also recorded.

Primary data has also been collected from the religious scholars. Because of time constraints main Jamiahs (Religious Institutions) of the city have been selected. The Muftis at Jamiahs have been interviewed, but names are not allowed to be mentioned.

Secondary data about fiscal structure, number of taxes and types of taxes on plots etc. has been collected. Sample estimation is carried out to find the net

loss/profit of the government in case of substitution of zakat for taxes in the study area. The information about sample estimation has been taken from property dealers of Peshawar city. Descriptive analytical technique is used to discuss the results of both primary and secondary information.

Scope of the Study:

The results of the study would be used to carry out further research on real property and zakat obligation in the province in particular and in the country in general. There is a need to make legislation to calculate and deduct zakat at source as taxes and many other things are deducted at source. This could be done with the help of National Data Registration Authority (NADRA) in Pakistan. There is a need to translate the research in Urdu so as to give awareness at local and grass root level.

Zakat and its Payment on Non-Agricultural Land:

Khalid Al-Qudah¹ in an answer to a question about zakat on plots replied that there is zakat on plots people possess. If a person has the intention to build a house on that plot there would be no zakat on that plot. Zakat is 2.5 percent annually based on the current market value of the plot. According to him if a person has no money to pay zakat he is not supposed to sell the plot but has to pay Zakat as soon as possible. Jakhura² also mentioned that zakat should be paid on the current market value of the plot if the plot is purchased for resale. In case it was purchased to earn a rental income, then zakat is not payable. Zakat would be then on the rental income.

Desai³ replied to the question of zakat on plot and explained that there is no Zakat on the plot for the past year one has kept it. Now when one sells the plot, the law of Zakat will apply on the proceeds of the sale. If one year passes on the amount of that sale, then Zakat will be compulsory on that. If already the person is Sahib-e-Nisab so the condition of one year is not there, he has to add this amount with other amounts and pay zakat on the whole amount.

The tax year in Pakistan is from 1st July to 30th June of the next year i.e. 12 months. According to Global Property Guide⁴, income from property is subject to presumptive tax. Presumptive tax is a tax where the income tax is based on average income instead of actual income. There is 5 percent withholding tax on the gross rent income of leasing property. There is no capital gains tax on gains realized by individuals from selling real property in Pakistan unless this real property is the part of his business. Property tax is at a flat rate in Pakistan. This rate is 10 percent in all areas except the province of Punjab. Capital value tax is another tax which is on the purchase of real property in urban areas at a rate of 2 percent on the property's value (or Rs.50 per square yard in case the value of property is not recorded).

Property is purchased to hold for long term rental income or gains or for speculative purposes. There are three different situations in which the land plots are purchased; people buy it to keep it for long and then to sell when its prices are high. Second, the land is purchased to build a house and third is the case where the plot/plots are purchased to sell them to get the money to buy a house. The first type is called purchase for resale. The second is for home consumption. In the third case sometimes more than one plot is purchased because the value of one plot is less than the expected price of a house so the individual goes for buying more than one plot, and then sells all these plots to get one house for his family. Lambat⁵ has quoted Dr. Yusuf Al-Qardawi, Dean of the University of Qatar as saying about the first kind and declares it a trade transaction and a commercial commodity so it is liable for zakat and the rate of zakat would be 2.5 percent. Since this is a commercial commodity so its value should be appraised on yearly basis. All jurists have this view because they consider it as “Wealth”, but the followers of Imam Malik hold that it should not be appraised on yearly basis but zakat would be paid only once when it is sold. At that time its current value is subject to zakat at a rate of 2.5 percent. In the second case the person has no intention to sell but to build a house. Then there are two situations; one in which he intends to give it on rent and second is to use it for his own family. According to Dr. Qardawi, if it is for family use then there is no zakat but if he gives on rent then zakat would be levied on the rental income. Lambat has further quoted the South African scholar Mufti Desai who is of the opinion that land purchased other than for resale purpose is not subject to zakat.

Adil Salahi an author and a scholar from U.K. as quoted by Lambat expresses that since these plots are meant for investment purposes because so far no construction work is started and if somebody offers you a price that is attractive so you will obviously sell it and from that amount you would buy another plot or property so it means it is a commercial property and is liable for zakat on the market value.

The Pakistan Accountant⁶ quoted Justice Maulana Taqi Usmani as saying that there is zakat on properties acquired for trading purpose and zakat would be at market value of the plot. If the residential plot is bought for resale then one has to pay zakat at market value but any purpose other than reselling zakat will not be payable.

Hakikat⁷ mentioned that Hadrat Ibn Abidin stated that if a person is keeping land plot for his own use but later on intends to sell it, it does not become commercial property. If he has obtained by inheritance present or alms and now wants to sell, these are not treated as commercial property.

The federal government of Pakistan has levied 2 percent capital value tax on the purchase of an urban property through Finance Act 2006. All Provincial Governments also imposed property taxes on the ownership of

property (no tax on the gains (capital gains tax) of the real estate unless for business purposes sale and purchase is carried out). There is also tax payment in the form of stamp duty by the provincial governments at the time of registration of the property. The rate of the tax is from 4 to 6 percent of the value of the asset. There is also another tax by the local government which is imposed at the time of purchase. The rate of this local tax is between 1-3 percent of the value of the asset⁸.

Dowall and Peter ⁹ mentioned that in large cities 20 to 40 percent of the land is owned by the government and rest is by the private sector. The median share of the property tax by the local government in Pakistan is 4 percent much below as compared to other developing countries which is 17 percent. They further mentioned that because of high stamp duties registration of real estate is discouraged. This rate of avoidance is about 50 percent. To avoid taxes they use Power of Attorney.

Sherazi ¹⁰ mentioned more than fifteen items on which zakat is liable including GP Fund, insurance but he has not specifically mentioned zakat on plots in the list of items.

Results and Discussion:

The opinion of the religious scholars teaching in the study area but graduated from different Jamiahs (religious institutions) shows the following results:

The scholars graduated from Akora Khattak are of the opinion that Zakat is mainly on three types of assets¹¹; Money and deposits, gold and silver assets and tradable assets. Plot is basically considered in tradable assets; hence, the principle of zakat for plots is same as that of tradable things. Zakat is payable and compulsory when one complete Islamic year passed on plot which is bought with the intension of trade. The amount is 2.5 percent of total monetary value of plot at the end of Islamic year, or its 1/40 of monetary value, it includes the taxed amount which is payable to the government.

Muftis graduated from Jamiah Wafaqul Madaris mentioned the same views as above but added that from the total value of the assets, tax amount must be deducted because that is a liability. After deduction of taxes, rest of the amount comes under zakat obligation.

The primary information further shows the following results¹²:

The sample population is 100 percent literate and is ranked among the high class i.e. from professors to businessmen and from doctors to engineers. The age group is selected above 25 years so as to avoid very young respondents. The head of the family usually pays Zakat so the choice is made for the head of

the family. The average plot possession is estimated 2 plots. However, sample population possess up to ten plots in some individual cases.

The level of unawareness is found very high among the general public in the study area. Out of total, only 39 percent of families pay zakat and the method of payment is onetime payment in the life of the asset. Rest 61 percent families neither pay nor have any knowledge about the payment. Many among them (15 percent) are landlords and holding many plots in posh areas worth millions of rupees but neither they nor their ancestors have ever paid zakat on any plot. Those respondents who pay zakat, their method of payment is not right in all cases; some pay in cash, some in kind like giving in the form of wheat or any other thing they have surplus but not measured accurately. The value of zakat obligation in terms of kind is subject to own calculation and choices of the people. The respondents are also of the opinion that since the zakat amount becomes a huge amount so we are unable to pay. There is another problem that if the head of the family is unemployed for years and have no cash to pay zakat on plots then how he has to pay, is a question that needs careful consideration.

Zakat collections could substitute the government budget expenditure from 21 percent of Annual Development Program during 1983-84 to 43 percent in 2004-2005¹³. According to Kahf ¹⁴, in Pakistan Zakat from gold and silver, money, livestock and agriculture is about 1.6 percent to the Gross Domestic Product (GDP), Zakat from salaries, rent of building and manufacturing is 3.5 percent of the GDP and from building and non-family used fixed assets is 4.4 percent of the GDP. According to Sherazi (1996), the potential zakat collection for these three categories are 1.5, 3.43 and 4.31 percent of GDP in Pakistan respectively.

There are about 39,000 local Zakat committees and more than 250 thousand volunteers in Pakistan¹⁵. Ministry of Religious Affairs collects zakat officially and is deducted mainly at source, for example, bank accounts, GP fund etc. People use to convert their fixed accounts into current, for they don't trust official channels. Zakat in Pakistan is collected by private sector as well but that depends on trust.

The total population of the sample study area was 1,116,641 on 1st January, 2011¹⁶. The estimated number of total plots in the sample area was 22,563. Total zakat collection in 2010-11 was 7,914,536 million rupees. The average plot and its price in the study area were estimated as Rs. 800,000. The tax revenue in the budget 2010 was 1,493,560 m. rupees. Direct taxes were estimated as Rs. 565,600 million. The taxes in the study area on plots by the local government were between Rs. 400 to Rs. 2,000 per month depending on the size of the plot¹⁷.

So value of plots on the basis of average estimation = number of plots × average plot price

$$= 22,563 \times 800,000$$

$$= 13,388,400,000$$

Total zakat on plots per year at 2.5 percent rate is = Rs. 335 million

Zakat as percent of direct taxes is = $335/565,600 \times 100 = 0.05$ percent

So if in a single city zakat collection is 0.05 percent of the total direct taxes of the entire country, it means that if all people pay zakat properly and regularly, there would be no need of imposing multiple number and high rate of taxes.

The on average contribution of zakat from non- family used assets in Pakistan is 4 percent of the GDP. The GDP stands for \$ 202.83 billion (estimates during study period), and 4 percent of GDP becomes 694.88 billion rupees, is an amount which could be enhanced to a greater extent i.e. approximately 10 percent to the GDP if proper fiscal system for zakat collection is introduced by deducting zakat at source on all fixed assets.

Conclusion and suggestions:

The level of payment of zakat on non-agricultural plots i.e. plots meant for trade in the study area is found below 50 percent. The awareness level is also low in the study area. So the hypotheses are rejected. The tax rates on plots are more than the rate of zakat so again the hypothesis is rejected.

Among the general public few families pay Zakat on plots. A large number of population has no idea about the payment. Those people who pay Zakat are not clear about the method of payment; some pay in cash, some in kind. Those who pay in cash they pay once in the life time of the asset whereas according to the rule since they have bought it for resale or investment purpose so they have to pay Zakat on its current value each year. Those who pay Zakat on kind basis, they have to calculate the value of that thing properly and equalize it with 2.5 percent of the current market value of the plot. However, if the person has no house of his own and the plot is purchased to be built a house there is no Zakat on it.

Further, it is allowed to deduct expenses on anything liable for Zakat. In case of plots the expenditure on plots including government taxes which are allowed to be subtracted and then Zakat should be given on rest of the value of plot.

There is another problem discussed that in case a person has no money to pay Zakat on his plot, from where he has to pay? Although some Ulama have said that he should not sell that plot but he has to pay Zakat. This case is very similar to gold a person is holding but unable to pay Zakat because of non-availability of money. In such a case, Shariah's ruling is to sell a part of gold and

pay Zakat. Since in case of plot one can't sell a piece or corner of a plot, Zakat payment is a problem. His plot is a commercial and tradable commodity so he should not keep such things and assets for which one can't pay religious obligations and refusal to Zakat is not allowed.

There is a case of keeping more than one plot for ultimately buying a house; the general opinion is that if these plots are so low in value that their combined value is less than or hardly equal to the value of a house being constructed for an "average family status" and "size" so keeping it for house construction is allowed because the family is waiting to sell the plots (say two plots) to build a house hardly or just enough to meet the family basic living requirements. But this method is not allowed for those who are keeping many plots to build a luxurious house.

There are different taxes on plots; property tax, wealth tax, local taxes etc. Their rates are also high. The results with the help of a sample calculation show that there is a great scope for zakat to be replaced with a number of taxes, only there is a need for introducing a proper system of Zakat collection. Since data base is there to check the sale and purchase of plots and also the asset is declared in income tax statements so it is easy to develop a full data record of the possession of these plots. The Muslim world should start fiscal reforms to steadily reduce taxes and implement zakat policy. The role of media is very important. In Pakistan, media is not actively participating in the campaign for creating awareness among the masses. In print media only importance of zakat is highlighted. Print and electronic media should advertise and explain the items of Zakat and its methods of payment. The government should prepare a comprehensive plan for the Islamization of the budgetary policy of the country.

End Notes

¹ Khalid Al-Qudah (2005). *Fatawa; Zakat on Inheritance*. available at <http://infad.usim.edu.my/modules.php?op=modload&name=News&file=article&sid=11763> retrieved on June 15, 2011

² Jakhura, Mufti S. (26 December 2010). *Zakat on Land*, Albalagh Newsletter, Retrieved on May 20th, 2011

³ Desai is a renowned South African religious scholar and Aalim and is quoted by Lambat in *How to calculate your Zakat* written by Ebrahim Iqbal Lambat and reviewed by Imam Uzair Akbar and Mufti J. Akbar, Holland Park Mosque Australia and also review by Imam Y. Patel of Jamiat-ul-Ulama South Africa, Published by The Lambat Trust Australia, 2005

-
- ⁴ Global Property Guide. (20th Oct, 2010). *Rental Income is Quite Low in Pakistan*. Available at <http://www.globalpropertyguide.com/> Asia/ Pakistan/Taxes-and-Costs) retrieved on May 20th 2011
- ⁵ Lambat, I. (April 25th, 2010). *How to Calculate Your Zakat Property*. Available at <http://www.docstoc.com/docs/35833954/How-to-calculate-your-Zakat> retrieved on June 1st 2011.
- ⁶ The Pakistan Accountant (July-Aug 2005). *Various Zakah Questions*. The Pakistan Accountant Journal, vol. 38 issue 4, July-Aug 2005, Chartered Accountants Avenue Clifton Karachi (Pakistan), pp: 10
- ⁷ Hakikat. (1998). *Endless Bliss*. Waqf Ikhlas Publications No: 5. Eighth Edition. Darussefaka Cad. No: 57/A P.K. 35 34262. Fatih-Istanbul/Turkey. Page 11 of 169 <http://www.hizmetbooks.org> retrieved on June 1st, 2011
- ⁸ Asim, A. and Shahid, R. (2009), *Investing in real estate Pakistan*. Grant Thornton International. Available at: www.gtpak.com/Documents/Real_Estate_Investment_Guide_Line.pdf. Retrieved on June 2nd, 2011
- ⁹ Dowall, D. and Peter Ellis. (November 2007). *Urban land and housing markets in the Punjab, Pakistan*. Working Paper 2007-04. IURD, Institute of Urban and Regional Development, Berkeley
- ¹⁰ Shirazi, N. S. (1996). *Targeting, coverage and contribution of zakat to household's income: the case of Pakistan*. Journal of Economic Cooperation Among Islamic Countries, Vol.17 (3-4). Pp:165-186
- ¹¹ Data collected from capital city Peshawar, June 2011
- ¹² Personal interview from the heads of the families (May 2011)
- ¹³ Hassan, M.Kabir, J. M. Khan. (2007), *Zakat, external debt and poverty reduction strategy in Bangladesh*, Journal of Economic Cooperation, 28, 4, pp.1-38
- ¹⁴ Kahf, M. (1989). *Zakat: Unresolved issues in the Contemporary Fiqh*, Journal of Islamic Economics, 2 (1), pp. 1-22.
- ¹⁵ Shirazi, N. S. 1996. *Targeting, coverage and contribution of zakat to household's income: the case of Pakistan*. Journal of Economic Cooperation among Islamic Countries, Vol.17 (3-4). Pp:165-186
- ¹⁶ www.trueknowledge.com/q/population_of_Peshawar_Pakistan_in_2010 retrieved on May 20th, 2011.
- ¹⁷ Property dealers, Peshawar City (June, 2011)