Maximise you zakah through a tax deduction

If you are a taxpayer in Australia, either your zakah can cost you less, or you can make a higher contribution.

Under Australian tax law, you will get a tax deduction if you make zakah (or any other charity) contributions to a zakah organisation that has DGR status. DGR stands for Deductible Gift Recipient. Many zakah funds in Australia have DGR status.

You can either pocket the tax deduction or contribute more charity, particularly in the month of Ramadan when the reward for your acts are multiplied.

How does it work?

How much tax deduction you receive depends on the highest rate of taxation that you are paying. This is referred to as your marginal tax rate (MTR). The more you earn, the higher your marginal tax rate.

Australian taxation rates, including medicare levy are as follows:-

Income	Marginal tax rate
$0 - $18,200	0%
$18,201 - $37,000	21%
$37,001 - $90,000	34.5%
$90,001 - $180,000	39%
$180,001 and above	47%

If you earn below $18,200; you are not paying any income tax and you will not receive any deduction for your zakah/charity contributions. If you have income above $18,200, you will qualify for tax deductions on your zakah/charity contributions made to a fund that has DGR status.

How much deduction you receive is dependent on how much income you have and how much tax you pay. Tax rates range from 21% to 47%. The higher your tax rate, the higher your zakah deduction.

If you have taxable income above $18,201 but below $37,000; your income in this range will be taxed at 21%. If you make a zakah contribution of $2,500 you will receive a tax deduction of $525. That means your zakah has only cost you $1,975. You can pocket the $525 or you can make a higher contribution to charity of $3,025 ($2,500 plus tax deduction of $525).

You will receive the tax deduction in your final assessment when the deduction is either set off against other income you have or you will receive a refund from the Australian Taxation Office (ATO).

If you have taxable income above $90,001 but below $180,000, you will qualify for an effective 39% tax deduction. That means you will get a tax deduction of $975 on a $2,500 contribution. The net cost to you would be $1,525. Once again, you can pocket the $975 or you can make a higher contribution of $3,475.

Given the need for Muslim aid globally, instead of pocketing your tax deduction, you should make a higher contribution. The cost to you is the same. The higher your contribution, the better the ability of the various zakah funds to address Australian and global needs.

The table below outlines, for the same $2,500, how much your tax deduction would be across the various income tax rates.

Marginal tax rate:	21%	34.5%	39%	47%
$2,500 donation	2,500	2,500	2,500	2,500
Tax deduction	525	863	975	1,175
Net donation cost	$1,975	$1,638	$1,525	$1,325

The higher your zakah contribution, the higher the dollar value of your tax deduction.

Below are the calculations for $5,000 and $10,000 contributions.

Marginal tax rate:	21%	34.5%	39%	47%
$5,000 donation	5,000	5,000	5,000	5,000
Tax deduction	1,050	1,725	1,950	2,350
Net donation cost	$3,950	$3,275	$3,050	$2,650
Marginal tax rate:	21%	34.5%	39%	47%
$10,000 donation	10,000	10,000	10,000	10,000
Tax deduction	2,100	3,450	3,900	4,700
Net donation cost	$7,900	$6,550	$6,100	$5,300

If your zakah payment is $5,000 then at a 21% tax rate the cost to you is $3,950. At a 47% tax rate, the cost to you is $2,650.

The net effect of the above is that you should factor in your marginal tax rate when you make zakah payments - this will result in a lower cost to you (which is acceptable in Islam) or you can make a higher contribution.

What you should do:

- Check if your preferred zakah fund has DGR status.
  Many advertise by stating that contributions are 100% deductible.
- Check your last tax return to see what your top income dollar was and based on the rates above, you can work out what marginal tax rate applies to you.
- Calculate your zakah and multiply your zakah by your marginal rate – the result is the dollar value of your tax deduction.
- Decide whether you wish to make an additional contribution or pocket the deduction.

Note: Ignored from the above calculations are any tax offsets that you may receive.

Companies also receive a tax deduction.

If all of this confuses you, you should speak to your accountant/financial adviser for more information on the impact of DGR status.
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