

Rotary Club Accounting and TAX issues.

To clarify these issues, we should ask ourselves some questions:

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Why do we have a Club and a Trust?

Answer – Liability, Taxes and Security

Some general things to note:

- In the eyes of the law and the IRD, Rotary Clubs are not charities.
- There is no LAW against running events/fundraising activities in the trust.
- It is important to be aware that your Club's Charitable Trust is a totally separate legal entity to the Club and needs to be administered properly.

Liability –

The CLUB is incorporated under the Incorporated Societies Act 1908. Under this act, all members are protected from liability in respect of any contract, debt, or other obligation made or incurred by the Club.

The TRUST. There are no similar provisions in the Charitable Trusts Act. So while registration of the club's Charitable Trust gives the trustees some protection from liability, the Act is not as clear cut as the Incorporated Societies Act and as a result, trustees could finish up being personally exposed should a project (being run in the trust) go terribly wrong.

Taxes-

THE CLUB Any entity or person who sets about to make a profit (and does) is liable to pay Income tax on that profit. The club is thus liable for income tax on all its INCOME. Any interest earned by the club AND most all of the club's profit making/fund raising exercises (such as film evenings, auction, sale of Christmas puddings, etc.) are income and subject to this tax law. No exceptions.

(Club activities with its members are mostly excluded. Payments from members to the club for dues, meals, sergeant and sunshine funds are not "income" for tax purposes, as they come from "inside the circle of membership").

We can cancel out any income tax liability (not GST if the club is registered) that a club accrues by managing what we do with the profits made. In assessing the club's overall tax liability, we are entitled up to a \$1,000 deduction to cover some expenses AND to deduct donations the club makes to a Donee organisation.

Donee organisations are charities, organisations registered with the Charities Commission and or organisations otherwise approved by the IRD to receive donations (and give tax effective receipts).

THE TRUST is a registered Charity and is thus a donee organisation. The Trust doesn't have to pay Income taxes.

Protecting the Funds

This is perhaps the most important issue. The club Charitable Trust should be the custodian of the accumulated funds raised by or donated to the club (or direct to the Trust) which should be kept completely separate from any liability the club may incur in undertaking projects.

As holders of the accumulated funds the Trust Trustees must not undertake any activity which puts those funds at risk - irrespective of the liability or otherwise of the Trustees. By running projects in the trust, those funds can be exposed.

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Best practice then, is that the Trust should not run projects!

Summary

Issue	The CLUB	The TRUST
Income Taxes	Liable to Pay	Not liable, no taxes
Liabilities	Protected	Not protected
Asset Security	Poor	Good
Projects	Run in Club	Does not run projects
Make Cash Donations?	NO	Yes

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The MONEY flow



Donate all Club Profits to the Trust BEFORE the end of the year.

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This leads to:

Organisational structure

1. We need to run the fund raising projects (and the other activities, such as camps, that are not “giving money away”), in the club in order to protect members against liability and financial losses.
2. If we give the fundraising profits (and other taxable income such as interest earned) away to a donee organisation such as our Trust, there is no income tax to pay (but the club has to file a tax return to ensure this).

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3. IF we make charitable payments/donations directly from club funds we CANNOT deduct that payment from the taxable income unless the recipient is an authorized donee organisation.
4. THUS we should not keep fundraising profits in the club and or over the club year end change, but donate them to the club's Trust.
5. Having donated all the profits away to the Trust, the TRUST should make the donations to the target recipients, NOT the club.
6. The reality is, with a few exceptions, the club "give money away" projects need to be/should be funded out of the Trust NOT directly from Club funds.
7. So, the function of the Trust is firstly to be guardians of the accumulated funds and secondly to actively facilitate the distribution of funds for the charitable purposes as defined in the trust deed and as approved by the Trustees. The trustees will usually review a list of requests presented to it by the Club Board.

Some special issues

Sergeants Funds

These are payments from members to the Club and generally exempt from all of the above, in both receipt and distribution.

District

Rotary Districts are not charities or Donee organisations. Requests from District for Donations/charitable projects should not be given to District out of club funds. Funding requests from District that are sourced from the Trust must be supported by a written guarantee as to their charitable use and distribution.

All overseas causes must go via RNZWCS - even if initiated by District.

WHAT is taxable income in a Rotary Club?

Some background

Clubs and societies have long been subject to income tax and required to file tax returns. But up until 2008 most Rotary clubs held a charitable status recognised by the IRD and were thus exempt from income tax and filing returns. With the introduction of the Charities Commission and the laws and rules surrounding those changes, clubs lost this exemption and consequently their reporting requirements and income tax obligation changed from 1 July 2008.

This is why the Club charitable trusts were created. Certain types of club income is assessable income and potentially will attract a tax bill at (currently) 28%. By donating the otherwise taxable income to a registered donee organisation (i.e. the club trust and any other REGISTERED charities), the donations become a deduction and negate the income tax liability.

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When the circumstances fit (i.e. the presence of assessable income) there is no exemption to the requirement to file an income tax return. Most clubs have some form of assessable income in each year.

So do Rotary Clubs HAVE to file a tax return?

NZ tax law establishes that tax is a self-assessment obligation. That is, it is a tax payers' responsibility to declare their position, not the IRD's responsibility to ask for it (even though they often do). So, the fact that you haven't been "asked" for a return, does not solve your problem.

It is interesting (to me anyway) that the IRD holds some contradicting views on some aspects of this. There are letters in circulation from IRD to some clubs that state if a club has less than \$1,000 in assessable income, they don't have to file a return. Their website also says that there is no need to file if your net income is less than \$1,000. There is no question that the \$1,000 deduction exists (it is prescribed by law) and clubs can claim it, but the IRD publishes contradicting instruction on its consequence: -

The general taxation principle is that there is a difference between an "exemption" and a "deduction". The \$1,000 is prescribed by law as a DEDUCTION (section DV8, Income tax act 2007). To claim a deduction you have to file a tax return.

The IR9 is the prescribed tax return for clubs and societies. In these documents and their explanations (IR9GU) the position is different. In these they say

"All New Zealand clubs and societies must file a tax return each year unless they derive only exempt income."

Further they state: **"Post us the return (even if there is no tax to pay)."**

So with a simple interpretation of the language there are some key words

"All"

"Must"

"Only"

All of which are hard to misunderstand!

We are left then with the **"Exempt"** bit (set out below).

There is a new IR9 published each year and the IR9 documents have remained consistent with this language since 2007 and are most likely subject to a higher level of quality control in their publication. It is thus our view that the IR9 language probably represents the true IRD position. That is, (contrary to the IRD letters) \$1 of interest and or \$1 of trading income generates the obligation to file a tax return, even if there is actually no tax to pay. Certainly it is the most conservative and safest position is to take this view and taking it does not detrimentally affect the club's tax position.

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With a proper accounting system in place, to work out if you need to file takes just a few minutes and having got that far, filling out the actual tax return is only another 30 minutes, so why not?

What is Income for tax purposes i.e. NOT exempt?

Any enterprise or activity intended to make a profit is classed as a business. If a club runs a business, it must pay tax on all profits after expenses (except those made on dealings with its members). (IRD definition)

Examples of income that is assessable:

- Investment income
- Interest
- Profits from all fund raising events
- Sale of tickets to events
- Sale of purchased goods
- Money received for services performed

Excludes sale of donated goods

What is NOT assessable income for tax purpose i.e. what IS exempt?

- Amounts received by a Club from within the circle of membership are not income for tax purposes. Examples:
 - Members subscriptions
 - Meal money
 - Sergeant's fines, shrapnel, etc.
 - Members donations
 - Raffles
- Amounts received by the club for/from:
 - Gifts and legacies
 - Donations of cash, goods or services
 - Money from the sale of donated goods
 - One-off sale proceeds from capital assets

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To help you decide what is and isn't assessable income, the table below is the IRD's own illustration of the classification of common income items.

Table of income types

	Liable for income tax	Not liable for income tax	Liable for GST	Not liable for GST	Exempt from GST
Subscriptions		✓	✓		
Donations		✓		✓	
Koha		✓ [†]		✓	
Bequests		✓		✓	
Grants		✓	✓		
Unconditional gifts		✓		✓	
Subsidies		✓*	✓		
Suspensory loans	✓		✓		
Trading activities	✓		✓		
Raffles or houseie proceeds		✓*	✓		
Admission fees	✓		✓		
Affiliation fees	✓		✓		
Sale of donated goods or services		✓			✓
Sale of purchased goods	✓		✓		
Sale of assets or equipment		✓	✓		
Insurance receipts		✓	✓*		
Hall or equipment hire	✓		✓		
Rent received (residential)	✓				✓
Rent received (commercial)	✓		✓		
Penalty payments (fines)	✓		✓		
Advertising or sponsorship	✓		✓		
Interest or dividends	✓				✓
Gaming machines	✓		✓		

* Liable in certain situations

† The tax treatment of koha depends on what it is. See our factsheet *Payments and gifts in the Māori community (IR 278)*.

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What is DEDUCTIBLE?

- A deduction is broadly defined as any expenditure or loss necessarily incurred in the earning of assessable income e.g.
 - the purchase price of goods sold
 - the cost of food at a fundraising dinner
 - Some of your club's expenses MAY be deductible (see note 1 below)

PLUS

- **gifts of cash to an “approved donee” i.e. your club’s TRUST (and any other approved donee organisation)**

What is NOT deductible?

- Any expenditure that is NOT necessarily incurred in the earning of income.
 - This will cover the costs associated with the day to day running of the Club, since they are not connected with the earning of assessable income
 - Any expenditure on capital assets
 - Any donation to a person that is NOT an approved donee

Within your club, the key to avoiding paying income tax is to have a process in place to donate any taxable income (profits) to your Club TRUST or any other donee organisation. Thus those profits become a deduction.

Note 1

Club expenses as tax deductible items.

Some club operating expenses (RI and District dues, admin costs such as computer expenses, audit etc) may be claimed as fundraising expenses IF there is a logical and rational reason for doing so. The IRD has suggested a pro rata apportionment based on the different income sources but other methods could be used should it be appropriate. Consistent application of the allocation methods used is required.

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Other Income Tax issues

Overseas payments

From a tax point of view, payments/donations to overseas causes are especially sensitive.

Unless they have a specific and special status (listed under Schedule 32 Income Tax Act 2007), clubs and regular donee organisations (INCLUDING your Trust) are NOT authorized to treat overseas payments as legitimate donations for tax purposes (and the donations will lose their tax deductible status). So, for example, if you make payments from your Club directly overseas you CANNOT treat that payment as a deduction against your club's assessable income and may finish up paying tax on it . even though you gave the money away.

To overcome this problem, Rotary has created an organisation called RNZWCS Ltd (Rotary NZ World Community Service) that is an authorised donee organisation for international purposes (listed in Schedule 32) that can receive donations from NZ clubs and Trusts AND is able to make overseas payments and have them retain their tax deductible status.

Thus, to achieve the appropriate tax effect, if overseas payments are paid to RNZWCS Ltd with the necessary instructions for them to pass the money on, you can make the payment from the trust or the club and not pollute its donee status and tax position.

Payments to The Rotary Foundation are sent overseas via New Zealand Rotary Clubs Charitable Trust ("NZRCCT") which has Schedule 32 status as well. ONLY Foundation payments are sent via NZRCCT and these should be made from your TRUST.

NOTE: Standard trust deeds for New Zealand Rotary club trusts (and the tax law) only permit donations to New Zealand causes . so in most all cases your trusts are NOT permitted to make direct overseas payments and you must use RNZWCS as your payment vehicle.

What is a DONATION?

This is an important question as it has direct tax consequences for both a Rotary Club and a Trust (if it is registered for GST)

A donation is exempt both income tax and GST.

Definition: A DONATION is something given freely without any expectation of anything in return. Any whiff that there is a benefit received and it is NOT a donation.

So, for a club,

Donations received are not taxable income provided they meet the above test.

Clubs can make donations to anybody, but only those made to donee organisations can be treated as a tax deduction. Donations to the club trust (and in most other circumstance)

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must be made in cash (actually paid out) and deposited into a bank account separate from the club (i.e. not under the control of the club).

For a Rotary trust

From an income tax position, donations made and received are exempt income and not subject to income tax.

If, however, a trust is registered for GST, careful assessment of the genuineness of a donation is important. GST is a tax on **goods and services**. If there has been any benefit given in exchange for the money then the amount exchanged will be subject to GST and GST must be collected and accounted for. For example, if a trust provides parking for an event and asks for a **donation** in exchange for that, a service has been provided and GST will become part of the transaction.

While it is legitimate to split a parking fee into **services** and **donations**, it is a grey area as to establish what is the market rate of parking and creates an arguable issue. It is easier to avoid all of this (and potential liabilities) by collecting the money in the club and donating it all to the trust.

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