Taxation of Clubs and Associations – don't be "teed" off at tax time

Understanding your tax obligations is not always easy. In fact, the term "tax simplification" seems to be an oxymoron. It can, however, be even more difficult to grapple with for those managing the tax affairs of a club, society or association. This is because although several income tax exemptions exist, they may not always apply. You are then stuck with determining exactly how your not-for-profit organisation will be taxed.

Are you dealing with a charitable organisation? Are you involved with an "amateur sports club"? If not, what are the rules governing your organisation, is the organisation truly a not-for-profit body?

You may have heard the quote "in golf, as in life, it is the follow through that makes the difference." This resonates at many levels. In the taxation world, we know that without careful planning and forethought unexpected tax bills can arise.

Where your organisation is a registered charity an income tax exemption is available for both business and non-business income. An exemption also extends to certain fringe benefits provided to employees. To attract these exemptions, the business must be carried on for charitable purposes. "Charitable purpose" is defined to include "the relief of poverty, the advancement of education, the advancement of religion, or any other matter beneficial to the community". However, these are legal tests and there is a rigorous application process one must go through to apply and gain registered charity status with DIA Charites Services (the regulator of charities in New Zealand).

Where your organisation or club is not a registered charity it may still be entitled to an income-tax exemption. Amounts derived by any club, society, association or trust established mainly to promote any amateur game or sport may also be exempt, for example golf clubs would be one such example. This exemption is available provided no part of the income or funds of the club are available to be used for the private pecuniary profit of any proprietor, member, shareholder or beneficiary. In reviewing what the main purpose of a sports club might be, the Commissioner of Inland Revenue would look to all the surrounding circumstances, including the organisation's constitution or trust deed and activities carried on for a particular tax year.

What if your organisation is not a registered charity or amateur sports club but is still considered "not-for-profit"? In this instance, the not-for-profit organisation will not be exempt from income tax. It could however be considered a "mutual association". The mutual association rules cover a wide range of organisations and include any society, association or organisation that is not carried on for the profit or gain of any members or shareholders. It is also important that the association's rules prevent it from distributing any property or money to any member or shareholder.

A mutual association, whether incorporated or not, is one that has a common or mutual purpose and can include a wide range of organisations such as trade associations, body corporates, chartered clubs and professional bodies (note this does not include friendly societies which are afforded their own income tax exemption and also have their own governing Act of Parliament. Essentially any entity that is not formed to make profits, but to further the interests of their members are captured. The organisation's constitution or founding document must include relevant clauses to ensure that the not-for-profit objectives are set out. This includes clauses covering payments to members and ensuring that no private benefit is received and that a member cannot influence the amount of any payment. The organisation must also include a winding up clause which normally requires surplus funds to go to a club or association with similar objectives, or to a registered charity.

A mutual association is not fully exempt from tax and it is only certain income derived from within the "circle of membership" that is not taxable. This is referred to as the mutuality principle. Such income as subscriptions for membership and levies charged to members are examples of income that is not considered gross income for tax purposes.

However certain types of mutual transactions such as the sale and purchase of trading stock and the supply of services to members are deemed taxable as statutes of law in New Zealand overwrite the mutuality principle for certain types of transactions. Consequently, income from conferences and sponsorship income will be subject to tax as will passive income such as income from the rental of premises. It may be difficult to categorise some transactions and mistakes in treating these income streams incorrectly can be costly. Hence professional help could be beneficial in order to ensure that the organisation is neither underpaying nor overpaying tax.

Any expenditure incurred in deriving member income that is not taxable will, of course, be non-deductible. Apportionment of general expenditure may be made on a pro-rata basis where the not-for-profit organisation derives both taxable and non-taxable income. In addition, a specific deduction is available for up to $1,000 of non-member net income.

Tax obligations can also extend to volunteers in these organisations. Generally, amounts derived by a person from voluntary activities are taxable income, unless the amounts received are reimbursement payments for expenditure incurred by the volunteer.

Where a payment to a volunteer exceeds the actual cost incurred, the payer must treat the excess as an honorarium. An honorarium is a "scheduler payment" from which tax must be deducted at the rate of 33%. From 1 April 2017, non-employees receiving scheduler payments (contractors) can elect their own withholding rate to better match their tax payments to their income, subject to a 10% minimum rate applying for residents.

In conclusion, there are many exemptions that may apply to your organisation. They don't however apply across the board to all not-for-profit organisations so it is important to know exactly where your organisation fits into the provisions outlined above.

About the Author

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