



Anglican Church Diocese of Sydney

ST. ANDREW'S HOUSE SYDNEY SQUARE NSW 2000
ALL CORRESPONDENCE TO:
PO BOX Q190 QVB POST OFFICE NSW 1230

TELEPHONE: (02) 9265 1555

3 April 2013

CONFIDENTIAL CIRCULAR

Dear Minister and Wardens

New tax ruling for School Building Funds

Purpose of this circular

1. The purpose of this circular is to explain the likely impact of a new tax ruling (TR 2013/2) issued by the Australian Tax Office ("ATO") in relation to the endorsement of school building funds as deductible gift recipients ("DGRs") and to make a number of recommendations both in respect to existing and new school building funds. It does so under the following headings –

Background

What are the requirements of the new tax ruling?

Multi-purpose buildings

Transitional arrangements

Consequences of non-compliance

Recommendations

2. Since this circular is directed to all Sydney Anglican parishes, we necessarily take a conservative approach in framing our comments. If your specific arrangements fall outside our general recommendations, you may wish to seek further advice to determine if your specific arrangements nonetheless comply.
3. It is important to note that the 'school' activities and building arrangements in each parish will differ, sometimes considerably. This circular does not take specific circumstances into account other than where indicated.
4. It should also be noted that this circular does not comprehensively outline all of the compliance obligations that apply to the operation of school building funds.

Background

5. A number of parishes operate school building funds that have been endorsed as deductible gift recipients (DGRs) by the Australian Tax Office (ATO). Endorsement as a DGR means that donors can claim a tax deduction for their donations.
6. School building funds can be used to raise funds to acquire, construct and/or maintain certain facilities that are used for the purposes of a school. A school may include, for example, Sunday School (and the like), ESL classes and the Moore College PTC course, among other educational activities. School building funds have been used by various parishes to raise funds to acquire, construct and/or maintain halls and multi-purpose buildings that are used, at least in part, for these purposes.

7. At the end of 2011 the ATO issued a new draft tax ruling on school building funds for public comment (TR 2011/D5). The former ruling (TR 96/8) was withdrawn. A key concern with TR 2011/D5 was that it proposed to replace the test in TR 96/8, that buildings must be used predominantly for the purposes of a 'school' (the "50% use test"), with a test that buildings must be used solely as a school and any other use must be minor or occasional. This would have potentially disqualified a large number of parishes from using the school building funds they presently operate, since while their buildings would be used for the purposes of a school more than 50% of the time, it would not be true to say that they were solely used for the purpose of a school and non-school use was minor or occasional.
8. The ATO received a number of submissions arguing that its approach was not consistent with the law (including a submission from the Anglican Church Property Trust Diocese of Sydney).
9. On 13 February 2013 the ATO released a final tax ruling on school building funds (TR 2013/2). The ATO has abandoned the sole use test proposed in the draft ruling.
10. A copy of TR 2013/2 can be downloaded at –
<http://law.ato.gov.au/atolaw/view.htm?docid=%22TXR%2FTR20132%2FNAT%2FATO%2F0001%22>

What are the requirements of the new ruling?

Building used as a school

11. The first requirement is that there must be a building that is used as a school. The new ruling does not apply a 50% use test or a sole use test in respect to the use of that building, instead the ruling provides (in summary) that –
 - the use of the building as a school must be substantial,
 - non-school use must not be of a kind, frequency or relative magnitude as to preclude the characterisation as a school,
 - any non-school use must not materially limit, detract from or otherwise be incompatible with school use,
 - where a church carries on a school it is relevant the extent to which the school is able to control the use of the building, and
 - the building must not be adapted in a manner which prevents it from being regarded as a school as a matter of ordinary language.
12. The adoption of this test in replacement of the 50% use test is the most significant difference between the former ruling and the new ruling. Quantitative matters such as –
 - the time the building is used as a school as opposed to non-school use,
 - the number of people involved in the school as opposed to non-school use,
 - the physical area put to school use as opposed to non-school use, and
 - the extent of any modifications to accommodate non-school useare relevant factors in assessing whether the tests summarised in paragraph 11 are met but they are not determinative on their own.
13. In the past, so far as the question of building use was concerned, it was enough to demonstrate that school use would occupy 50% or more of the time that the building was in use. The test is now more complex and less objective. Elements of whether non-school use detracts from school use, whether school use has priority over non-school use and the general character of the building will now be considered by the ATO.

School Organisation

14. The second requirement is that there must be a “school organisation” with its own distinct identity which provides regular, ongoing and systematic instruction in a course of non-recreational education. According to the new ruling, the following factors are indicative of there being a school organisation –
 - the organisation has a quality of permanence,
 - it has a governing body which controls its affairs,
 - it has a set curriculum,
 - instruction or training is provided by suitably qualified persons,
 - the enrolment of students,
 - some form of assessment and correction, and
 - the attainment of a qualification or status that is recognised outside of the organisation.
15. It is important to note that these are indicative of a school organisation. It is not mandatory that all factors to be present for there to be a school organisation. For the most part, these requirements are very similar to those in the former ruling, although there are some differences.
16. The ruling indicates that the school organisation will ordinarily have its own name, be an institution in its own right (even though it may exist within a broader institution or organisation) and have a governing body which controls its affairs. The new ruling would appear to go further than TR 96/8 in this respect. However the distinct identity requirements largely reflect the existing law that has been established by the courts in relation to what constitutes a school. TR 96/8 simply referred to the school organisation being an “institution” whereas the new ruling provides greater elaboration as to what this has been held to mean by the courts. For this reason it is unlikely that the distinct identity requirements in the new ruling will herald a new approach by the ATO.
17. The new ruling gives examples of scenarios that will qualify as a school organisation and scenarios that will not.
18. One example of an arrangement that the ATO will accept involves a Sunday School that –
 - is run by a separate committee under the terms of a church’s constitution,
 - operates in accordance with specific rules,
 - keeps separate accounts and records,
 - is run by appropriately qualified teachers,
 - the teaching is done in accordance with a set curriculum
 - the committee has control over the building used for Sunday School,
 - the children are registered, assessed on what they have learned and receive certificates that enable them to progress to new levels of learning.
19. Another example given of an arrangement in the church context that the ATO will not accept as a school organisation is as follows –
 - only children whose parents attend church each week and class size vary considerably from week to week,
 - there is no attendance register,
 - the classes are based on topics developed by the teachers,
 - the teachers are members of the church who have a calling or interest in children’s ministry but no apparent qualifications, and
 - there is no formal assessment.
20. It is difficult to know how much to deduce from these examples since they tend to outline opposite ends of the spectrum in assessing whether arrangements in a church context will be accepted by the ATO as a ‘school’. In reality most scenarios in our parishes are likely to be somewhere in between.

21. Nonetheless the greatest area of distinction between the two examples is perhaps the extent to which the arrangements for the school have been formalised and documented.
22. If you have a school building fund, it would be advisable to put some documentation in place to formalise the operation of your school organisation. In many cases it may be enough to simply document what you already do and require in relation to your school activities. For example –
 - *Appropriate qualifications:* This does not necessarily mean qualifications in education or theology (or tertiary study in other relevant subject matter). We understand there have been instances where the ATO has accepted the diocesan safe ministry course as a sufficient qualification for a Sunday School teacher.
 - *Enrolment:* Keep an attendance register.
 - *Curriculum:* Document the plan of lessons and objectives. If you use the Youthworks' CEP materials this will be relatively easy.
 - *Control of building:* Have the parish council resolve that the Sunday School has prioritised use of the building (at least a certain times).
 - *Accounting:* If feasible maintain a separate account and document a process for payment of Sunday School expenses
 - *Governing body:* Constitute a committee from among the Sunday School leadership and give it responsibilities in relation to the operation of the Sunday School.
 - *Attainment:* Progressing through levels in your curriculum. If the children receive a prize in recognition of their Sunday School involvement (perhaps a Bible at the end of the year or on graduation from Sunday School) this could also be documented.

Multi-purpose buildings

23. Many parish building projects now involve the construction of multi-purpose buildings or buildings in multi-purpose complexes. The former ruling provided little detail on the approach the ATO would take with respect to multi-purpose facilities. By contrast the new ruling includes quite a detailed explanation and outlines the process the ATO will take when assessing such proposals.
24. Each multi-purpose building or building (or in some cases part of a building) in a multi-purpose complex must be separately identified and assessed against the tests outlined above to determine whether it is a school building. A school building fund can only be applied to meet the acquisition or construction costs of buildings that are school buildings.
25. If a school building has not been materially adapted or specifically designed to accommodate non-school use, the school building fund can be applied to meet the entire costs of construction or acquisition.
26. If there are adaptations or design features to accommodate non-school use, and their cost is material, the school building fund cannot be applied to meet those costs. So far as possible the actual cost of the adaptation or design feature should be determined on a fair and reasonable basis. If this has not or cannot be done apportionment is required based on a fair and reasonable estimation of the extent to which the adaptation or design feature contributes to the total cost. The ruling gives an example of a common area which has significant design features that are intended to accommodate non-school use.
27. A similar approach is taken with respect to maintenance expenses. A school building fund cannot be applied to pay the cost of maintenance that is attributable to the building's non-school use if that cost is material. If the actual maintenance costs arising from non-school use has not or cannot be ascertained apportionment is required based on a fair and reasonable estimation of the extent to which the buildings non-school use contributes to the total cost of maintaining the building.

Transitional arrangements

28. The new ruling contains transitional arrangements for school building funds that were endorsed prior to 13 February 2013. However these are limited in several respects.
29. The former 50% use test will continue to apply to arrangements for the acquisition or construction of a building which a fund *became committed to* before 13 February 2013. In such cases the factors set out in paragraph 11 will not apply and the question will be simply whether on a quantitative assessment the building is used as a school for more than 50% of the time.
30. The new ruling defines “became committed to” as including a fund which has before 13 February 2013 –
 - (a) accepted significant donations or contributions relating to the acquisition or construction arrangements; or
 - (b) incurred, or become legally required to incur, significant financial costs for the purposes of entering into or carrying out such arrangements.
31. The transitional arrangement would apply to an arrangement for the acquisition or construction of a building where a building contract or other contractually binding arrangement has been entered into by or on behalf of the parish prior to 13 February 2013 which is to be expensed against its school building fund (and those expenses are significant).
32. It would also apply in circumstances where no legally binding commitment has been entered into prior to 13 February 2013 but significant donations have been accepted prior to 13 February 2013 in anticipation of a project to acquire or construct a school building. In such a circumstance there is a commitment to those donors to proceed.
33. The new ruling does not give a threshold above which expenses or donations are regarded as “significant”. The ordinary meaning of “significant” is something that is of substance, importance or consequence. Therefore the amounts do not need to be overly large but they must be more than merely nominal.
34. The definition of whether a fund “became committed to” a building project is inclusive. This means there may be circumstances other than those stated in the ruling that constitute a fund being committed to an arrangement for the acquisition or construction of a building. In some circumstances it may be necessary to obtain further advice.
35. If the transitional arrangements do not apply this does not necessarily mean that your fund does not comply with the new ruling. It simply means that the factors set out in paragraph 11 above apply to your fund in place of the 50% use test. It is quite likely that where the 50% use test is met, the test set out in paragraph 11 above would also be met.
36. The transitional arrangements also apply to the provision of money by a fund to maintain a building before 1 July 2013. This means that, regardless of your circumstances, the test set out in paragraph 11 above will apply to any donations for maintenance purposes that are received after 1 July 2013.

Consequences of non-compliance

37. Parishes have an obligation to self-assess their entitlement to continue to operate a school building fund once it has been established and to advise the ATO if the fund ceases to be entitled to endorsement. A failure to do so can lead to prosecution. You should pay close attention to the requirements in the applicable parts of the tax rulings where there will be or has been a material change of circumstances in the school activities of the parish since endorsement.

38. The ATO can revoke a fund's endorsement as a DGR if it considers the fund no longer meets the requirements for entitlement. This revocation can take effect when made or retrospectively. In such instance the fund may need to be wound up and accumulated donations paid to another fund in accordance with the wind up provisions in the fund rules.
39. If a fund's endorsement as a DGR was revoked retrospectively, donors would lose the benefit of having made tax deductible gifts and may receive amended income tax assessments from the ATO. However it is extremely unlikely that the ATO would issue an amended assessment in circumstances where a donor has acted in good faith and had an honest belief that the fund was entitled to endorsement at the time the donation was made. In any case usually the ATO can only amend the tax assessments of individuals within two years of the date of assessment.
40. Nonetheless, the potential consequences of non-compliance can be significant. It is therefore very important to continually assess your entitlement to endorsement regardless of whether or not the transitional arrangements apply.

Recommendations

School building funds in existence prior to 13 February 2013

Committed to arrangements to acquire or construct a school building prior to 13 February 2013

41. If your parish has a current project to acquire or construct a school building, to which it is committed, either through having received significant donations before 13 February 2013 or having entered into legally binding arrangements before 13 February 2013 requiring significant expenditure, and your circumstances have not changed materially since the fund was endorsed, we suggest you continue to fundraise for your project through your school building fund.
42. If you wish to continue operating a school building fund but there is doubt about whether you have attained the requisite commitment to rely on the transitional arrangements or there is doubt as to whether your circumstances have materially changed since endorsement, you should seek further advice to determine whether the transitional arrangements apply and, if they do not, whether any of the additional requirements in the new ruling alter your entitlement to operate a school building fund. The first question to ask will be whether your use of the building as a school accords with the factors set out in summary form at paragraph 11.

Proposal to acquire or construct a school building but not committed to do so prior to 13 February 2013

43. If your parish has established a school building fund in anticipation of acquiring or constructing a school building, but as at 13 February 2013 had not received significant donations or entered into legally binding arrangements requiring significant expenditure, the safest course would be to assume that the additional requirements in the new ruling apply to your fund. You will not be able to rely on the 50% use test and will need to assess your use of the building as a school against the factors set out in paragraph 11.
44. Depending on your circumstances it may be advisable not to commence fundraising and to seek further advice on whether any of the additional requirements in the new ruling alter your entitlement to operate a school building fund.

School building funds not in existence prior to 13 February 2013

45. If you are applying to the ATO after 13 February 2013 or have a pending application, the application will be assessed by the ATO against the terms of the new ruling.

46. If your application is pending, you may wish to submit further information to the ATO in relation to the new requirements (in particular those set out in paragraph 11). You should seek advice from the lawyer or other person who prepared your application before doing so.

All school building funds

47. It is strongly advisable that you formalise and document arrangements for the operation of your school organisation so that you can readily demonstrate to the ATO that there is “school organisation” with its own distinct identity which provides regular, ongoing and systematic instruction in a course of non-recreational education and that the relevant test for use of the building by this school organisation continues to be met. See the section titled “School Organisation” above, in particular paragraph 22.
48. We would appreciate receiving feedback from any parishes that have applications approved or declined after 13 February 2013 as this will assist us to ascertain how the ATO is applying the new ruling.

Contact

49. Any parish wishing to discuss these matters or provide feedback about their experiences with the ATO is encouraged to contact me. My contact details appear below.

STEVE LUCAS
Manager, Legal Services

T: 9265 1647 | M: 0423 850 067 | F: 9265 4485
E: szl@sydney.anglican.asn.au | www.sds.asn.au