

## Understanding Exempt Benefits

This benefit is a very specialised piece of legislation that only applies to pastors, making it quite unique. Also, despite there being a legislative framework for Exempt Benefits in the Frings Benefits Tax Act, the ATO has given very little guidance as to how such benefits ought to be administered or controlled. And yet, Exempt Benefits are exceptionally valuable. If a Senior Pastor is paid according to the QB Remuneration Guidelines, they would receive an extra \$13,460 per annum cash in their pockets due to this facility.

Beginning with stating the legal case for eligibility for “Ministerial Exempt Benefits, we need to look at Section 57 of the Fringe Benefits Tax Assessment Act 1986. This defines a series of conditions that must be met for a payment made to a pastor to be considered an “exempt benefit”. Reading legislation can often require a whole lot of legal training, but in this instance the wording itself is not all that complex. It states:

“Where:

- (a) the employer of an employee is a registered religious institution; and
- (b) the employee is a religious practitioner; and
- (c) a benefit is provided to, or to a spouse or a child of, the employee; and
- (d) the benefit is not provided principally in respect of duties of the employee other than:
  - (i) any pastoral duties; or
  - (ii) any other duties or activities that are directly related to the practice, study, teaching or propagation of religious beliefs;

the benefit is an exempt benefit.”

Or if paraphrasing and removing the double-negative in the fourth point it might end up saying:

Where:

- (a) a church is a registered religious institution; and
- (b) the pastor is a religious practitioner; and
- (c) a stipend is provided to the pastor or their family; and
- (d) the stipend is for doing pastoral or other religious duties;

the benefit is an exempt benefit.

Take for instance, a simple scenario, “A church appoints a pastor to undertake pastoral duties, then they can provide them with exempt benefits.” Or in a QB context, we would therefore point out that a Registered Pastor serving at a Constituent Church can receive exempt benefits. No problems! But what if it wasn’t a constituent church or what if the person was not a registered pastor? This is when the definition of the terms in this section of the Act might need some closer attention.

### **Firstly – what is a registered religious institution?**

This definition has updated in recent times to reflect the impact of the ACNC. The definition refers to institutions that are a “registered charity; and are registered under the ACNC Act 2012 as an entity with the purpose that is the advancement of religion.” If your church has registered with ACNC in accordance with the guides we have previously published in Network, there is no problem there. But

if you have chosen not to register with ACNC, then your church cannot provide exempt benefits to its Pastors. And if a person is employed by a For Profit entity, again they would not be eligible.

### **Secondly – who is a religious practitioner?**

The definition of this term provides four alternatives: The person can be “a minister of religion; or a student at an institution who is undertaking a course of instruction in the duties of a minister of religion; or a full-time member of a religious order; or a student at a college conducted solely for training persons to become members of religious orders”. I’d summarise this as ‘a pastor or a trainee pastor’. You can see that registration with QB ticks this box easily, but it could also apply to unregistered pastors. Training and calling are critical issues to consider – for example if you have not completed any recognised biblical studies, it would be hard to meet this definition.

### **Thirdly – what are religious duties?**

This is elaborated on in the clause itself as “activities that are directly related to the practice, study, teaching or propagation of religious beliefs”. The key question is whether the role influences the religious practice of entity. This is perhaps the most controversial of the three points. We have interpreted it to mean that people performing administrative tasks (even including the organising of functions of a religious nature) are not eligible, but people involved with or influencing the nature of these activities would be eligible.

The important issue with this definition is that all three of these definitions must apply to ensure eligibility for exempt benefits. Thus –

- A pastor working for a church in an administrative role would not be eligible.
- An untrained person working in a church in a religious capacity would not be eligible.
- A pastor performing pastoral responsibilities in a corporate or non-religious charity would not be eligible either.

Where eligibility is not clear, there is the option of requesting a private ruling from the ATO on the matter. Paperwork about the nature of the entity, the person and the job must be submitted, but this would then give a definitive ruling where there was any question.

### **Application Issues**

Ministerial Exempt Benefits are a mechanism by which a church can give a benefit to a pastor without needing to pay tax. Perhaps to illustrate with an example: if you are in secular employment - imagine if one day you wanted to buy a new television, and your boss says “I’ll buy that for you and just pay you a bit less this month”. He sends you out to buy the TV on his credit card, then only deducts the purchase price, net of GST from your gross wage. Your taxable income drops significantly so you pay much less tax. In fact you have just avoided paying PAYG tax and GST on the TV, and a \$3,000 purchase may only reduce your income by \$1,800. This might sound very unusual, but it is not at all illegal - in fact it is envisaged in tax law. Your employer has just provided you with what is referred to as a fringe benefit. There is an entire act of Federal Parliament dealing with this: the Fringe Benefits Tax Act 1986. So while your boss can do this for you, your employer then needs to pay Fringe Benefits Tax (FBT) on the transaction. FBT is calculated so the amount of tax equals or exceeds the amount of

savings if you just purchased the TV for yourself using your after-tax pay. In other words, no-one saves anything, but there is a lot of paperwork to do! Considering this – most employers do not offer such a deal.

But for pastors, thanks to the legislation discussed, such benefit is exempt and no FBT is payable - so the pastor can get the benefit, and the church doesn't get penalised.

This represents a considerable benefit, especially considering there is no legislatively defined limit in dollar or proportional terms. Such a generous scheme is wide open for abuse, and there are instances where this has occurred. To address this, most denominations have developed guidelines as to how Exempt Benefits are to be used. A similar benefit for employees of Public Benevolent Institutions was later capped in the legislation because of widespread over-use. Across many denominations, including Queensland Baptists, these recommendations are very similar.

For QB, we recommend that a level of remuneration is determined for a pastor based on a benchmark figure we provide each year, with some increases pertaining to experience and qualifications. It is recommended that 50% of the agreed figure is paid as normal taxable income, and the balance may be taken as exempt benefits. Why 50%? It is our view that this is a reasonable compromise position that takes advantage of this benefit while not pressing so hard as to make it feel like it is being abused. It probably represents a good objective to limit spending to this proportion of income while the balance is saved for a "rainy day". The proportion is not legislated, but it is the same figure that all state Baptist Unions recommend as well as many other denominations and is now widely established in the sector.

There are a few specific issues to note:

**(a) The benefit can be any goods or services.**

The ATO's examples (notably in tax ruling 92-17) only talks about housing, cars and school fees, but these are not an exhaustive list. A pastor eligible for exempt benefit may literally purchase any items they desire and claim them as exempt benefits if they choose. Historically, QB has produced lists of "suitable" items which may be funded from Exempt Benefits but we have stopped doing this as a pastor's individual circumstances will dictate what they need to spend money on at various stages of their lives – and the legislation is open ended. You can buy any goods or services and claim as a benefit.

**(b) The 'Can't Do's!**

- You can't take exempt benefits as cash. If you like to carry \$80 or so in your pocket to cover incidental expenses involved with life, then you need to draw this down from your normal pay, and NOT your exempt benefits. Of course, in theory you could draw \$200, then buy \$200 worth of goods and keep the receipts for that – but this is really messy. Far better just to not take it as cash, and purchase your goods and services using a credit card linked directly to the exempt benefit account. Not sure how? Baplink can assist you with setting these things up, so that you can be sure you have all the processes covered.
  
- You cannot surreptitiously (secretly) take it as cash. The most common such option is to use your exempt benefits to make home loan repayments into a mortgage facility with a line of credit or draw-down facility which allows you to re-access the funds. The exempt benefits have correctly been used to fund the housing repayment, but you have tricked the system by

drawing it back. A similar “trick” can be performed by purchasing goods which you then on-sell or return for a credit. Most stores will only refund you back into the same account anyway, but this approach is inappropriate to get around the restrictions on exempt benefits.

- You cannot give the money away. This includes your tithe to the church. You must pay this out of your normal pay, NOT your exempt benefit account. The reason is that a gift does not receive anything in exchange – there is no good or service that you receive for that gift. So, it does not comply with the regulations.
- You cannot transfer exempt benefits to another account. Again, a transfer to another bank account is a transaction where there are no goods or services received, and therefore it is not an eligible transaction. But, you might argue, I intend to buy things with it from the other account. I admit, you could do this... but this would require some very complicated paper work and it is far better simply to avoid this complication.
- You cannot save up your exempt benefits. Well, in practice you could – if you had something big you were about to buy in a year or so’s time. For example, to purchase the airline tickets for a big overseas holiday, you could save up your exempt benefits and use it for this. But don’t just let your funds accumulate. The problems start if you decide to leave your ministry context, and there is a large sum in your exempt benefit account. They cannot transfer it for you or give it to you – so the only alternative would be to tax it when it is being transferred. Far better to simply keep using it and keep the balance low.

To regulate all these in our guidelines would be overkill – instead we simply ask Pastors to be respectful of the regulation that exempt benefits are not taken as cash.

**(c) The exempt benefit is not actually income to the pastor, but an amount they may use to obtain benefits.**

This has significant consequences. It means for example that the exempt benefit component does not need to be declared on your tax return. But it may also mean your bank may not be comfortable with counting that amount in your income when you are applying for a home loan. We deal with some of the specific implications of this in the Remuneration Guidelines and again this has been a subject of several previous Network articles.

**(d) “Unspent” exempt benefits are not actually the Pastor’s money, but still the church’s money.**

The pastor therefore cannot regard them as an asset, and by rights the church ought to. This is another good reason to not allow the funds to build up in an exempt benefit account – especially at the end of a financial year. Hence we encourage pastors to use their exempt benefit amounts and not let it build up (unless you have a specific significant expense coming up). You do not need to feel tied to the 50% recommendation from us. This is only recommended as a maximum, so if it is accumulating and you cannot spend it, then simply agree to reduce the amount of exempt benefits you are receiving.

**(e) Record Maintenance.**

If a church was audited by the ATO, they could legitimately ask to review how Exempt Benefits are being handled. Churches are therefore responsible for ensuring good records of the use of exempt benefits are maintained, although they often out-source this responsibility to the pastor. The practice

of accurate recording and diligent maintenance cannot be overemphasised. There is a responsibility to keep a paper trail for all money spent – copies of receipts or credit card statements – that can clearly demonstrate how the benefits are used. One of these days, one of the churches will be audited by the Tax Office and the question will be asked.

While legislative provision for Exempt Benefits has been made, as outlined above there is very little regulatory support for how this legislation applies, and even less (effectively none) about the practical implementation. Thus, this final step is assumed to be the responsibility of the church and pastor to work out for themselves. To this end – QB has provided input through the Remuneration Guidelines document with details in how to process these amounts.

### **Exempt Fringe Benefits for Pastors – Processing Exempt Benefits**

How should a church and pastor should handle EFB's? There are no ATO guidelines about this, so any procedure for handling EFB's need to be developed by the organisation providing them. To this end, the ASG Committee has proposed three recommended ways to do this, and they are published each year in the Remuneration Guidelines.

We do not intend to repeat the step by step instructions contained in the Remuneration Guidelines, but the options here match the options in that document if you want to see some more specific guidance.

#### **Option 1: Pastor-Managed**

The pastor self-manages the use of their EFB's and must keep records in case of an audit. This enables the pastor to use their benefit in their own way without the need for disclosure to any other party, and makes it as easy as possible for the church, but it does place an administrative burden on the pastor.

In this option, the church determines the dollar amount that will be allocated to the pastor for EFB's, generally on the 50% rule recommended in the Remuneration Guidelines. This amount is paid into a bank account that the Pastor (and usually a spouse) are signatories to. The account ought to include the name of the church as well to remind everyone it is actually still church money until it is spent. The Pastor then spends the money how they choose, self-assessing whether all purchases are compliant with the EFB rules. The Pastor keeps a record of everything that is spent which is sufficiently detailed that they can demonstrate that no cash has been taken from the account. The Pastor keeps these records themselves but must be willing to share them if the church was to be audited (even if they have left the church). Records must be kept for a minimum of 7 years.

In this option, no tax invoices are required, and no GST is claimed back by the church. The Pastor therefore does not get full value for their EFB's, but they do maintain their privacy. It is worth noting also that a suitable account for this can be arranged through Baplink, as commercial banks might not understand how the account is supposed to work.

#### **Option 2: Church-Managed**

The church maintains the EFB funds and only pays them upon provision of a tax invoice by the Pastor. The church must shoulder the administrative burden in this option, but Pastors can enjoy the GST

benefits of this approach. Pastors must, however, provide full disclosure of all purchases they wish to claim.

In this option, the amount of EFB allocated to the Pastor is credited to a fund in the Church Accounts. The Pastor is told how much is available, and may submit a tax invoice for any purchase and have the full amount reimbursed. The Treasurer would need to ensure that the claims made were for eligible purposes. While reimbursing the full amount, the Treasurer would only debit the net amount (without GST) to the Exempt Benefit account, and claim the GST back on the next BAS statement. The Church would retain all the paperwork in case there was an audit at some point.

### **Option 3: Hybrid Model**

The church holds the EFB funds, and pays them out on provision of a credit card statement listing claimable expenses. This ensures the church maintains the funds and has some control over ensuring they are used appropriately, but the Pastor has some privacy about how the payments have been used.

In this option as in Option 2, the amount of EFB allocated to the Pastor is credited to a fund in the Church Accounts. The Pastor is told how much is available, but in this case may submit a credit card statement indicating the amounts he wants reimbursed. Ideally this ought to be an independent credit card not used for other purposes, although it could be the Pastor's general credit card with the payments for reimbursement marked. The Treasurer can determine that payments were for goods and services and not cash advances, so ensure the rules are being complied with. But as no tax invoices are supplied, the Pastor does not have to disclose what they are purchasing, only the total amount with each provider. The full amount is reimbursed, and the full amount is debited to the exempt benefit account (including the GST). The church then has and can keep all the records required in the case of an audit, but no claim for GST can be raised as tax invoices have not been obtained.

The important things to remember is that someone must keep records in case of an audit, and you can only claim the GST if tax invoices are obtained and provided to the church.

### **Exempt Benefits – What can they be used for?**

Some key issues that need to be considered:

(a) Exempt benefits can be used for the purchase of any goods and services but the money cannot be taken as cash

(b) Records to demonstrate the use of these accounts need to be retained for up to seven years. Tax invoices are not necessarily required, but credit card statements showing that no amounts were taken as cash must be retained.

(c) However, some churches choose to claim the GST on purchases made using Exempt Benefits. As our Remuneration Guidelines indicate, if this is being done, then the pastor ought to receive the benefit of this. If this is being done, then full tax invoices do need to be submitted to the church records in addition to the records kept in point (b) above.

(d) Exempt benefits ought not be used as “savings accounts” with the balance increasing over time. Earning interest on the account could be deemed to be taking a cash benefit. Ideally, the account balance ought to be reduced to \$0 at the end of each financial year, unless there is a specific significant expense about to fall due.

### **Does the Exempt Benefits need to be “ministry related?”**

We frequently receive questions about what Exempt Benefits can be used for, and if expenditure from a pastor’s Exempt Benefit account needs to be in some way ministry related. The reality is that it does not. Income received by way of Exempt Benefits may be spend on any goods and services you wish – and to repeat: it cannot be taken as a cash benefit. This has been clarified in the Remuneration Guidelines document published by QB on an annual basis – the last one was released in June 2017. It states;

“Exempt Fringe Benefits may be used for any incurred personal expenses of the pastor, but not taken in cash. Historically lists of “eligible” uses have been published, but there is no legal re-restriction on the use of exempt benefits. However, in stressing that the benefit cannot be taken in cash, this includes payments to accounts where the pastor has the ability to draw down that benefit as cash – such as a line of credit on a home, or cash advances on a credit card.”

On the same issue: it is worth noting also that to be strict, Exempt Benefits ought not be carried over from one financial year to the next. I have been presented with stories of pastors who have been saving up money in their exempt benefit account to remarkable levels. A strict interpretation of this would be that the exempt benefits are being used as a cash investment earning interest, and that would contravene the tax rules. Please aim to spend your exempt benefits in the financial year they are earned, so this matter won’t receive any undue attention. This is part of the reason why QB, and other major denominations do not recommend taking more than half of a pastor’s remuneration as Exempt Benefits – so they have the freedom to save for their future financially using the cash portion of their remuneration. If you receive Exempt Benefits and have a large sum in your account, please see if you can expend this money prior to 30th June to avoid any such concerns.

Baplink offer a facility through Westpac using a Purchasing Card (looks and feels like a credit card). The cards can be restricted to align with exempt benefit account rules and the statements will meet the documentation requirements as well. Please contact Baplink on [baplink@baplink.org.au](mailto:baplink@baplink.org.au) or call 07 3354 5611 if you would like any further information about this product.

### **Exempt Benefits for Pastors - FAQ - Frequently Asked Questions**

Exempt Benefits for pastors is a confusing issue for many churches. We have compiled the most frequently asked questions to assist with this pro-cess.

#### **1. Who should administer the accounts?**

The account can be administered by the Church Treasurer, reimbursing the pastor for receipts provided, or by the pastor themselves who keep all the records. Either way is ok. If the church administers the accounts, there is a GST advantage to be gained, but it is sometimes inappropriate for

pastors to have to provide all their documentation to the Treasurer. Both approaches are detailed in the Pastoral Remuneration Guidelines document, available on the QB web site.

## **2. What can I spend the money on?**

It is still commonly considered by pastors that you have to spend the money on ministry related matters, or housing or motor vehicles. This is not the case. The legislation indicates the money can be spent on any goods and services, but NOT taken as cash.

## **3. Do I need to keep receipts?**

Strictly, all expenditure from such accounts requires receipts. However, if a pastor was using a credit card or account dedicated to being an exempt benefit account, a detailed statement on that account would probably suffice. This would be sufficient to demonstrate that the entire amount has been spent on goods and services and not taken as cash. However, to my knowledge, this point has never been tested by an audit by ATO.

## **4. Can I save the money up?**

It is strongly recommended that you do not save up Exempt Benefit amounts, but spend this amount first before you spend your cash. Churches ought to undertake a reconciliation process at the end of each financial year, and ensure that all the money transferred into the exempt bene-fit account has been spent. If at the end of the financial year, or if you were finishing up from a ministry position, any lump sum in the account cannot be paid out directly as this would be deemed to be taking the benefit in cash.

The alternative is to pay it out and tax it – which would defeat the purpose of having the exempt benefit account. Of course, you can save whatever you want out of the taxable component of your remuneration, and if you are intending to save more than this – you ought to instruct the church to reduce the amount of exempt benefit and increase your cash remuneration.

Baplink offer a facility through Westpac using a Purchasing Card (looks and feels like a credit card). The cards can be restricted to align with exempt benefit account rules and the statements will meet the documentation requirements as well.

*Please contact Baplink on [baplink@baplink.org.au](mailto:baplink@baplink.org.au) or phone 07 3354 5611 if you would like any further information about this product.*

*Of course, if you have any questions or need further help, please do not hesitate to contact Administrative Services – [dapa@qb.org.au](mailto:dapa@qb.org.au) or phone 3354 5618.*