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**Submission from Our Community in response to the  
Consultation Paper on the Taxation of Australian not-for-  
profit organisations.**

Please find enclosed our submission.

Yours sincerely



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01 Find Money

02 Manage Money

03 Jobs

04 Marketing

05 Boards

06 Training

07 Insurance

08 Suppliers

09 Join the Directory

10 Communities in Control

11 Leadership

12 Advocacy

13 Technology

14 What Works

15 Community Calendar

16 Our Consumer Place

# THE TAXATION OF AUSTRALIAN NOT-FOR-PROFIT ORGANISATIONS

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## PRELIMINARY

This round of consultation is approximately the sixteenth we have been asked to attend to in the past three years.

Once again, we are being asked to comment on one small portion of the total picture without knowing what the other parts of the picture are likely to look like.

Once again, the scope of the consultation overlaps with our response to earlier queries (it is to be hoped that the Inquiry will go back over submissions to previous Inquiries to check out what has been said that might be relevant).

Once again, we are being asked to suggest minor tweaks to a historically contingent suite of legal forms and legal relationships. No legal form has ever been discarded, which means that no historical decision has ever been reconsidered and no assessment of need rescinded.

If the government sincerely wishes to set the not-for-profit sector on a sound footing, we believe it should urgently assign the responsibility for overseeing all changes to the sector to a single minister supported by a properly funded and nationally based departmental team. Only a properly co-ordinated and directed effort can produce a coherent and consistent outcome.

In relation to this (and all) consultation processes, we strongly urge that wherever possible the government returns to first principles, asking itself:

1. What outcomes do we wish to see?
2. What measures would lead to these outcomes?
3. How can these measures replace existing arrangements?

rather than the more limited "What changes can be made to existing arrangements to reduce their attendant inefficiencies?"

If the government wants to reduce the complication and confusion of the not-for-profit tax system it is going the wrong way about it. At present, the ATO handy hints table looks like this; this is as simple as they can get it.

Tax Concessions	Not-for-profit organisations	Community Service organisations	Charities	Public Benevolent Institutions	Religious Institutions	Deductible Gift Recipients
Tax-free threshold	✓					
Income Tax exemption		✓	✓		✓	
DGR status				✓		✓
Refund of imputation credits			✓			✓
FBT Rebate		✓	✓		✓	
FBT Exemption				✓		
GST NFP Concessions	✓					
GST Charity concessions			✓			✓
GST Religious concessions					✓	

Leaving the grid intact and asking what we should put in the boxes will get us nowhere. If we want to make this simpler, we have to start over with something more like this.

Tax Concessions	Groups doing things Australian society does not care about	Groups doing things for their members	Groups doing things Australian society cares about a lot
None	✓		
Some		✓	
A lot			✓

That would be simpler. Anything else – any fix that simply adds more exemptions or adds more exemptees – will be more complicated.

# CONSULTATION QUESTIONS

**Q 1** What criteria should be used to determine whether an entity is entitled to an income tax exemption?

1. Whether it is a not-for-profit or a social enterprise, as opposed to a commercial speculation:
2. Whether, and to what extent, it is for the public good.

**Q 2** Are the current categories of income tax exempt entity appropriate? If not, what entities should cease to be exempt or what additional entities should be exempt?

The current categories of exemption should be discarded and replaced by the criteria given above.

**Q 3** Should additional special conditions apply to income tax exemptions? For example, should the public benefit test be extended to entities other than charities, or should exemption for some types of NFP be subject to different conditions than at present?

The term 'charity' is one of the categories that we propose should be discarded.

The public benefit test should be the only test employed.

**Q 4** Does the tax system create particular impediments for large or complex NFPs?

Large and complex NFPs can, in general, look after themselves. Small and fragile NFPs need special consideration.

**Q 5** Should other types of NFPs also be able to claim a refund of franking credits?

If, and only if, strong regulation is in place to ensure that NFPs cannot accumulate funds indefinitely without spending them on their objects.

**Q 6** Should the ability of tax exempt charities and DGRs to receive refunds for franking credits be limited?

As above.

**Q 7** Should the ATO endorsement framework be extended to include NFP entities other than charities seeking tax exemption?

The classes of NFP entity should be entirely recast, and widened to include social enterprises.

Q 8 Should the income tax exemptions for State, Territory and local government bodies be simplified and consolidated into the ITAA 1997?

Yes. Any simplification of the current impossibly complicated system will relieve some of the pervasive anxiety affecting many organisations in the sector.

Q 9 Should the threshold for income tax exemptions for taxable NFP clubs, associations and societies be increased?

Yes. The current low threshold brings into the tax net many small organisations that do not contemplate that possibility at all and are thus technically in breach. A level of five thousand would seem reasonable.

Q 10 Please outline any other suggestions you have to improve the fairness, simplicity and effectiveness of the income tax exemption regime, having regard to the terms of reference.

Our Community's general suggestions are given in the introduction above.

Q 11 Should all charities be DGRs? Should some entities that are charities (for example, those for the advancement of religion, charitable child care services, and primary and secondary education) be excluded?

DGR status should accrue not to particular classes of entity but to organisations that can demonstrate public benefit.

Q 12 Based on your response to Q11, should charities endorsed as DGRs be allowed to use DGRs funds to provide religious services, charitable child care services, and primary and secondary education?

Where public benefit can be demonstrated.

Q 13 Would DGR endorsement at the entity level with restrictions based on activity address the behavioural distortions in Australia's DGR framework?

No. DGR status should accrue not to particular classes of entity but to organisations that can demonstrate public benefit.

Could unintended consequences follow from this approach?

Well, yes, but the same could be said for any government action, without exception.

Q 14 If DGR status is extended to all endorsed charities, should this reform be implemented in stages (for example, over a period of years) in line

with the PC's recommendations, or should it be implemented in some other way?

It should be extended in stages to allow for education of the sector.

Q 15 Would a fixed tax offset deliver fairer outcomes?

From the point of view of the sector, a fair outcome is one that enables organisations to do the maximum good work, and therefore encompasses the highest feasible donation level.

Would a fixed tax offset be more complex than the current system?

Perhaps the contrary.

Would a fixed tax offset be as effective as the current system in terms of recognising giving?

Tax concessions are seldom at present seen as 'recognition' of the value of giving, rather as arcane financial balancing. The difference would not be noticed.

Q 16 Would having a two-tiered tax offset encourage giving by higher income earners?

Only at the margin (though even a small increase could be significant for some organisations)

Q 17 What other strategies would encourage giving to DGRs, especially by high income earners?

Federal Gift Aid, following the UK model.

Q 18 Should testamentary giving be encouraged through tax concessions?

Yes.

Q 19 Would a clearing house linked to the ACN Register be beneficial for the sector and public?

Our Community has had a decade's experience in operating an online donation scheme for Australian community groups - GiveNow. Our Community does not charge for this service. Based on this experience, we would make the following observations.

a) While the current restrictive definition of 'charity' prevails, many worthy community groups do not have charitable status. This does not, we contend, mean that their objects are less valuable, and we require of groups joining GiveNow only that they be a legal entity and hold an authority to fundraise.

The existence of a donations clearinghouse under the aegis of the federal

government would tend to make it easier to give to charities than to other worthy causes, giving more rather than less weight to this historical shibboleth. Only if the definition of charity was greatly extended or if the ACNC were able to extend its ambit to all not-for-profit entities would this bias be removed.

- b) The statement that “108. Smaller charities are likely to have limited or no online fundraising facilities, and are therefore likely to benefit from this option” overlooks free services such as GiveNow. Rather than conducting the clearinghouse in-house, the government might consider funding existing private sector services.

- Q 20 Are there any barriers which could prohibit the wider adoption of workplace giving programs in Australia? Is there anything the Working Group could recommend to help increase workplace giving in Australia?

A Gift Aid program on the British model would add meaningful incentives to what is at present an almost unnoticeable administrative convenience.

- Q 21 Do valuation requirements and costs restrict the donation of property? What could be done to improve the requirements?

When considering DGRs, the requirement that only “*property valued by the ATO at more than \$5,000*” should be deductible should be discarded as irrelevant. A gift is a gift. For purposes of pure administrative convenience, the gift level might be set at \$50.

- Q 22 Is there a need to review and simplify the integrity rules?

Yes. In particular, the “\$150 or 20%” rule has the effect of making any return practically impossible.

- Q 23 Are there additional barriers relevant to increasing charitable giving by corporations and corporate foundations? Is there anything the Working Group could recommend to help increase charitable giving by corporations and corporate foundations?

Greater education for NFPs on gaining commercial partnerships, along the lines of Our Community’s helpsheets on [Community-Business Partnerships](#).

- Q 24 Are the public fund requirements, currently administered by the ATO, either inadequate or unnecessarily onerous?

Nobody now can say that the fund requirements are inadequate because no attempt has ever been made to flush out abuses. If they were inadequate, we would not know. Our Community is not aware of any complaints that fund requirements are too onerous.

Q 25 Are there any possible unintended consequences from eliminating the public fund requirements for entities that have been registered by the ACNC?

Well, yes, but the same could be said for any government action, without exception.

Q 26 Should the threshold for deductible gifts be increased from \$2 to \$25 (or to some other amount)?

Yes. The \$2 level is objectionable because it suggests to the average Australian that \$2 is a meaningful gift rather than an administrative irritation and a net loss to the donee after administration and banking costs are calculated. A level of \$50 would send a better message,

Q 27 Outline any other suggestions you have to improve the fairness, simplicity and effectiveness of the DGR regime, having regard to the terms of reference.

See Introduction.

Q 28 Assuming that the current two tiered concessions structure remains (see Part B), what criteria should determine an entity's eligibility to provide exempt benefits to its employees?

The voluntary sector as a whole underpays its staff and partially compensates for this by tax concessions, and the concessions should not be removed as long as the existing salary deficit continues.

Q 29 Also assuming that the current two-tiered concession structure remains (see Part B), what criteria should determine an entity's eligibility to provide rebateable benefits to its employees? Should this be restricted to charities? Should it be extended to all NFP entities? Are there any entities currently entitled to the concessions that should not be eligible?

As in all such questions, public benefit.

Q 30 Should there be a two-tiered approach in relation to eligibility? For example, should all tax exempt entities be eligible for the rebate, but a more limited group be eligible for the exemption?

All such questions depend on the system used to attest to public benefit.

Q 34 Should there be a requirement on eligible employers to deny FBT concessions to employees that have claimed a concession from another employer? Would this impose an unacceptable compliance burden on those employers? Are there other ways of restricting access to multiple caps?

Before any such requirement is instituted we would wish to see some evidence that this represented a detectable problem. If the estimate of \$10m tax savings is balanced against administrative costs incurred, including costs both to the ATO and to NFP employers, the imperative for change seems comparatively feeble.

- Q 35 Should the rate for FBT rebates be re-aligned with the FBT tax rate? Is there any reason for not aligning the rates?

No reason for not realigning the rates is immediately evident.

- Q 36 Should the limitation on tax exempt bodies in the minor benefits exemption be removed? Is there any reason why the limitation should not be removed?

The limitation should be removed.

- Q 37 Is the provision of FBT concessions to current eligible entities appropriate? Should the concessions be available to more NFP entities?

As with all such matters, the criteria should be not-for-profit public interest groups.

- Q 38 Should FBT concessions (that is, the exemption and rebate) be phased out?

The voluntary sector as a whole underpays its staff and partially compensates for this by tax concessions, and the concessions should not be removed as long as the existing salary deficit continues.

- Q 39 Should FBT concessions be replaced with direct support for entities that benefit from the application of these concessions?

It would seem difficult for the Commonwealth to pay subsidies to all organisations currently employing the concession, and impossible for it to subsidise all comparable entities arising in the future.

- Q 40 Should FBT concessions be replaced with tax based support for entities that are eligible for example, by refundable tax offsets to employers, a direct tax offset to the employees or a tax free allowance for employees?

Yes. Such a system would be slightly more transparent and more flexible. The connection of NFP salaries to fringe benefits is misleading.

- Q 41 Should FBT concessions be limited to non-remuneration benefits?

No. In the NFP sphere at the present these concessions are regarded as equivalent to salary, and any change to this would mean that NFP groups could not find adequate salaries for their staff.

- Q 42 If FBT concessions are to be phased out or if concessions were to be limited to non-remuneration benefits, which entity types should be eligible to receive support to replace these concessions?

See Introduction. Policies should be based on public interest criteria, not entity types.

- Q 43 Does the existing fundraising [GST] concession create uncertainty, or additional compliance burdens, for NFP entities that wish to engage in fundraising activities that fall outside of the scope of the concession?

Yes. Most small NFPs are incapable of handling the complexities of GST law, and the number of NFP organisations liable to the impost should be minimised.

- Q 44 Would a principles-based definition of the types of fundraising activities that are input taxed reduce the compliance burden for entities that engage in fundraising?

Yes. Self-assessment would be considerably more convenient.

- Q 45 Should current GST concessions continue to apply for eligible NFP entities?

Yes. Most small NFPs are incapable of handling the complexities of GST law, and most larger organisations are to a greater or lesser extent supported by government, making their tax burden largely internal tax office churning.

- Q 46 Are there any other issues or concerns with the operation of the GST concessions in their current form?

It should be noted that the difficulties experienced by both the ATO and NFPs in dealing with such cases are considerably reduced by the undeniable fact that most small NFPs ignore their responsibilities in this area altogether, crossing their fingers and hoping for the best. If compliance increased the level of pointlessly wasted time would rise commensurately.

- Q 47 Would an opt-in arrangement result in a reduced compliance burden for charities that would otherwise need to apply apportionment rules to supplies made for nominal consideration?

Again, we believe that most problems in this area are avoided by a commonsense agreement to ignore the strict terms of the law.

Q 48 If an opt-in arrangement is favoured, would the preference be to treat the supplies as taxable or input taxed? Why?

See above.

Q 49 Is there an alternative way of reducing the compliance burden associated with apportionment for supplies made for nominal consideration?

See above.

Q 50 Should the gaming, catering, entertainment and hospitality activities of NFP clubs and societies be subject to a concessional rate of tax, for income greater than a relatively high threshold, instead of being exempt?

Public interest considerations would suggest that associations should be encouraged to reduce their incentives to encourage gaming and drinking among their members, and some measure along these lines would be desirable.

Q 51 What would be a suitable threshold and rate of tax if such activities were to be subject to tax?

The rate set should not be such as to place such a considerable burden on the net finances of associations as to place their continuation in jeopardy.

Q 52 Should the mutuality principle be extended to all NFP member-based organisations?

Yes. The social and medical benefits of bringing people together are well documented, and should be recognised in tax law.

Q 53 Should the mutuality principle be legislated to provide that all income from dealings between entities and their members is assessable?

The Question here does not seem to reflect the discussion in the text above it, and its intent is not clear.

Q 54 Should a balancing adjustment be allowed for mutual clubs and societies to allow for mutual gains or mutual losses?

In the event that the mutuality principle is given legislative form, such an adjustment should be applied.

Q 55 Is existing law adequate to address concerns about exploitation of the mutuality principle for tax evasion? Should a specific anti-avoidance rule be introduced to allow more effective action to be taken to address such concerns?

The information that would be needed to answer this question is not available.

Q 56 Are there any areas in which greater streamlining of concessions could be achieved?

[See Introduction.](#)

Q 57 Do you have any ideas for reform of NFP sector tax concessions within the terms of reference that have not been considered in this discussion paper?

[See Introduction.](#) [See Appendix #1.](#)

## DONOR ADVISED FUNDS

It's very hard for an Australian not-for-profit organisation to get tax deductibility for donations made to it. The laws are antiquated, the rules ambiguous, and the procedures legalistic and bureaucratic. The procedures are so restrictive, in fact, and so inflexible, that quite a lot of effort has been expended on ways to get around them. Charities, donors, and, yes, the government itself have colluded in the evolution of the Donor Advised Fund.

In the normal course of events a private citizen who wants to get a return on their generosity must give to an organisation that counts as a Deductible Gift Recipient (DGR). The DGR, in its turn, must spend the money only on DGRable – 'charitable', in the warped legal meaning of the term – objectives. If the DGR wants to pass the money on to a worthy cause, it has to be a cause that itself is a DGR.

That's tough. Suppose, for example, that Georgina, a well-off Australian, wants to do good in the world without all that confounded paperwork. The government wants to encourage philanthropy, up to a point – a dollar that the rich spend on the poor is a dollar the government doesn't have to – and thus allows Donor Advised Funds, like those run by Perpetual Trustees.

Perpetual Trustees Australia... is now pushing Donor-Advised Funds as the charitable gift fund of choice.

Perpetual's National Manager of Charitable Planning, said that the fund is for donors who don't want the formal legal responsibility of managing their charitable investment, or carrying out the administration or the compliance requirements for government reporting but at the same time want the ability to decide who will be the beneficiaries.

They say Donor-Advised Funds are typically structured as a public charity, which is more cost effective and far less cumbersome than private foundations. These funds typically have an initial minimum contribution of \$10,000. The administration costs in a Perpetual fund are 0.65%, or \$650 for every \$100,000.

Perpetual said that it will offer an on-line service to donors where they will be able to use a secure pin number to monitor the progress of their Donor-Advised Fund and then email instructions regarding their preferred beneficiaries to the trustees.

Community Foundations, too, operate as Donor Advised Funds.

Helen Imber from the then called Melbourne Community Foundation said MCF had been offering this flexible fund for some time with enormous success because it allows individuals the opportunity to make decisions about where their money goes.

Furthermore, the last government established a new legal structure for

exactly this purpose, and the number of these funds is growing fast.

Two popular legal structures that accept tax-deductible contributions and allocate to authorised causes are:

1. The Prescribed Private Fund (PPF). This is a private vehicle established by an individual or family that has tax office approval to accumulate capital and allocate income to eligible charities. This is the giving industry's equivalent of the DIY super fund.
2. The public charitable trust. This is a donor-advised fund that groups monies contributed by individuals and organisations and invests and allocates these based on their various mandates. These are the equivalent of the superannuation industry's managed funds. Each of these vehicles is required to distribute its earnings but can re-invest capital gains and franking credits. Depending on the investment strategy agreed this means that the initial contribution to a fund can result in many years of funding contributions to the ultimate cause.

The structure, in any case, is that instead of just giving money to, say, the Children's Hospital, Georgina gives her money to, say, The Australian Communities Foundation and tells them "Give it to the Children's Hospital." And here lies a possible problem. Whatever advantages Georgina gets from giving away that money come, at least in theory, from the fact that she's given it away – that she's actually let go of it. And if she's surrendered all the accompaniments of ownership to the ACF then the ACF can do whatever it wishes with that money, whatever Georgina says. That's what ownership means. If Georgina can still direct it to the Children's, then that means it is in part still hers, and that's not allowed.

That's why the Australian Tax Office (ATO) has rules. Specifically, the ATO says

#### ACCESSING FUNDING FROM DGRs

Your organisation may be able to access funding from DGRs that operate to provide funding to other organisations. Examples of such DGRs include:

- the Australian Sports Foundation, which issues discretionary grants to sporting organisations, and
- the Australia Business Arts Foundation, which facilitates funding for the arts through its Australia Cultural Fund.

Where money or other property is transferred to a DGR on condition that it is passed onto a particular organisation or event, the tax deductibility of the payment may be affected. Donors can make a request that the gift be directed to a particular organisation. Such arrangements will not prevent the payment from being a gift provided that the DGR:

- obtains in its own right the full value or benefit of the property donated, and

- is empowered and has absolute discretion whether to distribute the property to those organisations nominated by the giver.

## EXAMPLES

### Example 1

Alice is an avid supporter of her local AFL team. She sends a cheque for \$500 to the Australian Sports Foundation (ASF) with a letter stating that the amount is to be given to her favourite team. The ASF does not have discretion whether to apply the amount in accordance with the giver's wishes. The \$500 is not a deductible gift, as no benefaction has been conferred on the DGR.

### Example 2

Cecilie is a great supporter of the arts in her local area. She sends a cheque for \$500 to the Australia Business Arts Foundation (AbaF) with a letter stating that she would prefer that the funds be given to an arts organisation that supports visual artists in her region. AbaF has the discretion whether to apply the amount in accordance with the giver's wishes. The \$500 is a deductible gift, as benefaction has been conferred on the DGR.

That's why all Donor Advised Funds, whatever their form, have a clause in the small print that goes something like this one (from the Australian Documentary Foundation).

Whilst all preferences will be taken into account and assessed by the Board, foundations, corporations or individual donors cannot directly designate their grant to a specific documentary project.

Which is, when you think about it, pretty silly. The Donor Advised Fund is going to give the money to any legal organisation you nominate, because that's what it's for. The idea that the Board sits around at every meeting taking decisions on the most deserving object and only then looking at the donation form ("What do you know, we've picked the same charity as the donor again. Boy, what are the odds on that?") doesn't pass the giggle test. If the Fund didn't meet the donor's wishes it wouldn't be used again. Even the ATO examples sound pretty feeble. Do you really think Greg didn't claim a tax break on his gift? Do you really think the ASF turned him in?

This constitutes a theoretical problem rather than an actual problem because nobody apparently cares. You'd think that if the government wanted to produce an outcome that was forbidden by its own laws it would change the laws rather than setting up a transparent evasion and looking the other way, but there seem to be political gains of some description in not being seen to take the actual decision straight out.

It is to be hoped that the present inquiry resolves these concerns.