1 June 2015

Tax White Paper Task Force
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam,

Tax White Paper Process – Re Think: Tax Discussion Paper

Social Ventures Australia welcomes the opportunity to make a submission in response to the Re Think: Tax Discussion Paper.

Please find attached Social Ventures Australia's submission.

If Treasury wishes to discuss the matters raised in this submission further, please contact me on (02) 8004 6729 or ilearmonth@socialventures.com.au.

Yours faithfully,

Ian Learmonth
Executive Director, Impact Investing

Introduction

Social Ventures Australia (SVA) welcomes the broad and inclusive consultation that is being undertaken in the current tax reform process. SVA recognises the need to optimise tax revenue to fund vital government services through an effective and simple tax system. We also recognise, however, the unique role that the private sector can play in alleviating some of the constraints faced by government in social service delivery through impact investments and how tax changes could increase this activity. Two specific tax initiatives are proposed in this submission that would incentivise impact investments and grow the market so that private capital can more readily assist with delivering necessary services in our communities.

SVA notes that the Government is keen to hear from all interested parties on any issues regarding the tax system, including views on tax matters raised in other review processes, such as the Financial System Inquiry. SVA actively participated in the Financial System Inquiry and was pleased by the inclusion of impact investment in the final recommendations. SVA made several recommendations in the Financial System Inquiry prosecuting the need for Government to participate in the growth of the impact investing market so that greater social outcomes can be delivered to the community. One of the greatest levers that the Commonwealth Government can use to grow the market is through specific tax reform designed to stimulate the market.

This submission recommends the introduction of tax concessions for impact investments in qualifying social enterprises (direct or through an intermediary), social impact bonds and social and affordable housing projects. These recommendations will be framed in response to three questions raised in the Re Think: Tax Discussion Paper relevant to the growth of impact investing in Australia:

1. Are the current tax arrangements for the NFP Sector appropriate? Why or why not?
2. Under what circumstances is it appropriate for assistance to be delivered through tax offsets?
3. What, if any, changes could be made to the current tax arrangements for the NFP sector that would enable the sector to deliver benefits to the Australian community more efficiently or effectively?

Background

Social Ventures Australia works to improve the lives of people in need. We focus on keys elements to overcoming disadvantage in Australia, including improved education, sustainable jobs, stable housing and appropriate health, disability and community services.

By offering funding, investment, and advice we support partners across sectors to increase their social impact.

We are a not-for-profit organisation established in 2002 by The Benevolent Society, The Smith Family, WorkVentures and AMP Foundation.

In our first 12 years:

- We generated over $50 million of investment from philanthropists, trust and foundations and government into the social sector,
- We worked with over 80 social ventures like Beacon Foundation, Ganbina, STREAT and AIME, and distributed more than $20 million to support their work,

- We delivered $4 million of support through government and cross-sectorally funded social enterprise programs in ACT, NSW and QLD,
- We leveraged $4.6 million of private investment to match government funding into the SVA Social Impact Fund to support innovative social enterprises,
- We helped to broker $165 million of investment into early childhood learning to fund the non-profit consortium buyout of ABC Learning Centres to create Goodstart, providing 15% of Australia's early childhood places,
- We worked alongside UnitingCare Burnside on Australia's first Social Benefit Bond, with the NSW Government,
- We were the lead partner of a consortium providing advice and support to the WA Government to deliver the $10 million Social Enterprise Fund, and
- We delivered over 550 consulting engagements for over 300 clients to strengthen the non-profit sector.

SVA believes a new social capital market needs to thrive alongside traditional financial markets and we are keen to develop the new asset class of social impact investment as it becomes increasingly part of the mainstream.

1. Are the current tax arrangements for the NFP Sector appropriate? Why or why not?

The current tax arrangements favour charitable not-for-profit organisations, particularly those that have deductible gift recipient (DGR) item 1 status. Such organisations can benefit from payroll, income and GST tax exemptions and can also produce tax deductible receipts for those that donate funds to their operations. Organisations that deliver similar if not the same services under a social enterprise or social impact bond structure benefit from few of such tax exemptions despite often operating in a more sustainable manner.

The not-for-profit sector has changed dramatically in the last decade. With a shrinking pool of philanthropic donations and government grants many not-for-profit organisations have sought to establish social enterprises as a more sustainable means of delivering social services to the communities in which they work. At the same time, a greater emphasis on outcomes based contracting has stimulated growth in social impact bond financing for some of the larger service providers in Australia.

Social enterprises like all businesses require access to capital to operate and grow. Present tax arrangements do not provide any deductions, offsets or incentives to investors that could meet the capital demand in the social enterprise sector.

2. Under what circumstances is it appropriate for assistance to be provided for tax offsets?

Tax offsets should be provided in circumstances where the net benefit created from the behaviour encouraged by the tax offset outweighs the foregone tax revenue to the Commonwealth. Impact investments have the potential to generate critical social outcomes for those that need it most in our communities, yet the supply of capital for social entrepreneurs and social impact projects is in limited supply. Tax offsets could play a central role in encouraging investors to invest in enterprises as an added tax offset could compensate for the risk of the investment and improve the risk/reward equation by delivering a higher after tax return to the investor.

Tax offsets should be made available for specific investment scenarios; either investment in social enterprises (either direct or through an intermediary), social impact bonds and social and affordable housing projects. Each of these investment scenarios will be considered in more detail below.

3. What, if any, changes could be made to the current tax arrangements for the NFP sector that would enable the sector to deliver benefits to the Australian community more efficiently or effectively?

Two specific changes could be made to the current tax arrangements for the NFP sector that would enable the sector to more efficiently and effectively serve the Australian community. These changes relate to direct investment in social enterprises and social impact bonds and investment in social and affordable housing projects.

Tax Initiative #1 - Investment in social enterprise and social impact bonds:

A tax concession should be provided to investors who make investments in either social enterprises or social impact bonds. Social enterprises and social impact bond structures promote more effective and sustainable service delivery as they promote more commercial operations and less reliance on grants and donations. Ideally, investors should be able to offset the amount invested in a social enterprise against their assessable taxable income in the year that the investment is made and enjoy a tax exemption from interest repayments or dividends as they are repaid during the life of the investment. Capital gains tax should also be offset when the impact investment is realised.

In order for an impact investment tax offset to be regulated, clear qualifying criteria would need to be established. Australia should look to provide tax relief for impact investments in the same way as the tax relief scheme established in the UK[1]. The below summarises a proposal consideration in the Australian context.

Broadly:

- Income tax relief is available for the amount invested, to be deducted from the individual’s income tax liability in the year of investment;
- CGT relief is available by allowing CGT on chargeable gains to be exempt where the person liable to CGT invests the gain in impact investment; and
- Capital gains on social enterprise investments are free from CGT if the investment is held for three years.
- Dividends and interest received in respect of the social investment are non-assessable.

Social enterprises, social impact bonds and suitable intermediaries can qualify as an investee.

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[1] https://www.gov.uk/government/publications/social-investment-tax-relief-factsheet/social-investment-tax-relief

The organisation receiving the investment to qualify for relief should meet certain criteria and qualifying investments should include both debt instruments and all forms of equity.

Whilst we have not quantified the savings to the Australian Government and community for such tax concessions, sources state that similar changes in the UK are expected to generate an additional GBP 480m in social investment. To date, several social impact investments have been launched in the UK as a result of these changes.

Tax Initiative #2 - Investment in Social and Affordable Housing Projects

Australia is presently suffering from a significant social and affordable housing crisis which is perpetuating disadvantage in our communities. New housing stock is required to replenish dilapidated stock and meet the rising demand; however, funding from the State Governments is extremely limited and the commercial realities for community housing providers often make new development uneconomical.

To stimulate private investment in social and affordable housing a new social infrastructure tax offset scheme should be implemented so that investors would be able to lend at sub-market rates to incentivise developers to build new social and affordable housing stock. The proposed tax offset would apply to interest paid on approved housing bonds to be tax exempt in the hands of the lender and not tax deductible to the borrower. Almost all borrowers in the social and affordable housing sector are tax exempt and therefore the ‘tax benefit’ of the interest deductions is worthless. The intention of the scheme would be that lenders share this benefit of tax exempt interest in the form of lower lending rates to community housing developers.

A similar tax offset scheme has been successful in the US. The Federal New Markets Tax Credits and the Community Reinvestment Act were designed to increase the flow of capital to low socio-economic areas. Since 2000 over $31.1 billion in new market tax credit transactions have been reported. In 2013 $55 billion was channelled from banks to poorer communities through social investment under the Community Reinvestment Act.