SUBMISSION

RESPONSE TO THE DISCUSSION PAPER ON TAX CONCESSIONS FOR NOT-FOR-PROFIT SECTOR

FOR: NFP SECTOR TAX CONCESSION WORKING GROUP SECRETARIAT

THE TREASURY

LANGTON CRESCENT, PARKES ACT 2600

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OVERVIEW

LASA Q is a Queensland based not-for-profit (NFP) member organisation that has been established over two decades to represent providers of residential aged care facilities, community care organisations, retirement villages and pensioner rental facilities. It also operates a NFP Education Institute undertaking onsite and distance education and training for care and support staff working in the age care industry. It is part of the LASA national federation. In Queensland, the 350 membership base provides services and support across 800 sites around the state. They are predominately drawn from the NFP sector with many members in smaller regional and rural communities.

LASA Q welcomes the attention to this topic and the desire by the Not-for-profit Sector Tax Concession Working Group to ensure support is provided to assist the sector in their pursuit of the public good and, in the overwhelmingly majority of instances, to those in most need. Our interests are directed to services to an ageing population. The tension in promoting a level playing field and supporting competitive neutrality in Australia's market driven economy is understood. Nevertheless the unique contribution made by the NFP sector, especially where market forces do not operate, such as in regional and rural Queensland, must be acknowledged.

Put simply, a strong NFP sector has always been part of Australia's social fabric and the country has financially and morally benefited from the contribution made by it. It is critical that its' ongoing contribution is strengthened and not diminished with the establishment of the ACNC and work such as that being undertaken by your Working Group.

Over the last decade there have been significant reviews, inquiries and reports about the NFP sector. Their findings and submissions to the 2010 Productivity Research Report 'Contribution of the Not For Profit Sector' clearly described the valuable role the sector plays in the domestic economy and the scope and breadth of the sector. Repeatedly they point out a number of diseconomies and disincentives for the sector because of:

- Over lapping Federal and State/Territory regulatory regimes
- Inconsistent and 'opaque' regulatory framework
- Burden of compliance
- Confusion over the nature of the different categories of the sector
- Difficulties regarding the establishment of a NFP entity
- Unequal allocation of DGR status
- Reliance on the common law definition of charity to ascertain when entities are eligible for tax concessions
- Accounting Standards and Guidelines do not take into account the specific characteristics of NFP sector entities and their users which causes problems for smaller, less resourced entities

- Many philanthropic organisations are prohibited from donating to NFPs that are not endorsed for Tax concessions and hold ITEC status under Division 50 of the Income Tax Assessment Act 1997 (Cwlth).

Similar concerns are expressed by LASA Q members and in addition they make the following points:

- Increased compliance regime for any Federal Government subsidised service such as aged care services
- Reduced subsidies/funding relative to CPI and other appropriate indices which reduces the viability of the sector and diminishes its' ability to expand service provision
- Short term nature of funding base with apparent limited appreciation by Government about financing and financial administration practices required to reassure bankers of the business case for operations
- Policy determination without regard to State/Territory regulatory requirements
- Contracts requiring the return of any surplus so limiting the capacity to efficiently apply funding and enable investment to improve effectiveness or efficiency, such as in information technology and staff training
- Compliance regimes required for volunteers has resulted in a decrease in volunteers and an onerous responsibility on the entity.

The Discussion Paper:

The 57 specific questions identified in the Paper about existing tax concessions are broad and sweeping but are important questions to be raised to help iron out arbitrary anomalies in the current law. They require careful consideration and consultation with the industry to ensure the NFP sector is not exposed to the risk of reduced benefits. The Discussion Paper must also be considered alongside other related ACNC reform measures – for example, a statutory definition of a charity. These parallel processes must be in accord if the best outcome for the NFP sector, Government and the Australian community is to be realised.

Technical Issues on Income Tax treatments:

Our submission does not address the technical issues relating to income tax treatment per se for NFP entities. Rather LASA Q will note submissions made by those working in the technical areas such as the Institute of Chartered Accountants, Accounting firms and similar bodies - then we can respond accordingly, while noting that generally the accounting industry is sympathetic to the NFP sector. One comment that can be made is the need for Rulings implemented in practice to be put into legislation to improve certainty for the sector and to minimise disruption to operations especially with the smaller, less resourced NFPs. Certainty, consistency and consultation should be the bywords for any proposed changes brought about by tax reforms that affect the NFP sector.

For this reason LASA Q does not believe that it is constructive to limit the benefits that currently exist in the NFP sector. The NFP sector is recognised for the worthy work it performs for the public good and reducing hard won benefits would cause distortions in service provision and likely cause a higher call on the public purse which would result in more expenditure than the tax benefits provided.

This is especially so given the disparities between eligibility for tax concessions across state and territory jurisdictions. Harmonisation of tax concession definitions or classifications is a noble aim but the evidence is that states and territories jealously guard their sovereignty and are slow to reform. While state and territory governments should recognise the Commonwealth's tax concession endorsement of NFP organisations, reform only at the Commonwealth level will exacerbate compliance regimes and lead to more confusion especially in smaller organisations.

Notwithstanding the above, if change is mandated in the short term, there has to be adequate education and information provided to SMEs in the NFP sector. LASA Q recommends that the ATO's Visitation Program directed to educating small entities on taxation matters and compliance could be replicated for the roll out of any changes. LASA Q and LASA's other state offices could assist in facilitating such sessions for age services providers around Australia.

Taxation deductibility for gifts:

The existence of taxation deductibility for gifts to many NFPs is an important driver to encourage philanthropy and should not be removed. The current $2 threshold is low and the processing of a taxation receipt etc would more than offset the value of a $2 gift. For that reason, LASA Q supports the increase of the tax threshold for gifts to $25 and recommends that this is done in two tranches - one up to $10 and in a further two years up to $25. This is recommended on the evidence, as articulated in the 2010 Productivity Commissions report (Appendix H), that it is uncertain what impact the taxation threshold has on donor intentions. As such, there is little evidence that increasing the taxation threshold would reduce gift giving in any appreciable degree. For NFPs the success of gift receipts will be in how their entity is seen as worthy relative to other worthy causes.

Any efforts to increase philanthropy should be encouraged. Australia is a wealthy county with a proud tradition of giving to causes both domestically and internationally. Options to widen the philanthropy net should be facilitated, especially as Governments now seek to limit their expenditures in the NFP health and aged care services sector. LASA Q is supportive of Option 2.7 Establishing a Clearing House for Donations to DGRs in the Discussion Paper. This would facilitate individual taxpayers to view the ACN register for assistance and reassurance of the bona fides of a preferred entity and security in donating through the Register's website. This option is also supported based on the personal experience of a LASA Q senior manager of workplace giving in Canada which provides an excellent template for any such practice in Australia.

DGR Status:

LASA Q recommends that DGR status is extended progressively and incrementally consistent with Government's ability to support the program. Currently distortions in DGR have an impact on the NFP sector which results in inequity across it. A planned and staged program should not be beyond the purview of government.

Taxing Not For Profit Businesses in the NFP Sector:

The work to be undertaken by the ACNC is welcomed by LASA Q which has experienced a significant administrative burden over the past twelve months in meeting compliance requirements of the Queensland Office of Fair Trading (governing body of the Incorporated Associations Act), ASIC in relation to the Australian Business Names Register, and the ATO in relation to our ABN registration.

The ACNC intent to collaborate with the ATO and State departments is considered by LASA Q to be a significant positive step. The ability for NFPs to gain clarification on the eligibility and application of compliance requirements and tax concessions would be viewed favourably in the sector, as would harmonisation of governance requirements for the NFP sector. Specifically, LASA Q would support the extension of the ATO endorsement framework across the sector.

As a NFP with only one full time resource dedicated to financial management, HR, IT, contract management and governance compliance, the existing income tax exemption is a significant relief for the Association in terms of both financial sustainability and compliance burden.

While limiting the tax concessions to enable a greater spread of the national tax burden will, in theory, enable a more widely spread tax relief, it also will have major direct impacts for LASA Q and other NFP entities in the age services sector. Under the current concessions, operating surpluses for NFP entities, such as LASA Q and many of its' members, are reinvested in the age services they provide, enabling them to meet the imperative of keeping costs to clients at a minimum.

LASA Q acknowledges the perceived distortions in the overall economy if the NFP sector operates commercial activities and is exempt from income tax that a commercial entity would be required to meet.

As a NFP member based Incorporated Association, LASA Q is currently exempt from income tax and is eligible to provide FBT salary packaging to its' employees up to the $30,000 cap as well as additional benefits related to meals and entertainment facilities. In addition to member services related to advocacy, policy development and compliance and governance support, LASA Q operates a professional conference organiser (PCO) service as well as a registered training organisation (RTO) providing aged care related vocational education and training. The commercial nature of these activities is clear, however, the critical point of difference is the NFP mandate to reinvest available surpluses and not distribute to stakeholders or members.

The reality is that in many instances commercial enterprise subsidises other activities in the NFP entity. For example, any surplus realised from retirement village operations are likely to be reinvested in supporting other charitable endeavours or subsidising services to those of very limited means. In member organisations, profits realised are returned to other loss making members' services provided. In the case of LASA Q's RTO and PCO functions, surpluses from these activities are directed to subsidising the core member services functions and supporting the administrative non income generating activities necessary to keep the Association operating. Where surpluses allow, investment is also made in additional training such as supporting staff from rural and remote sites to undertake training or offering training or member support in small rural areas that could otherwise not be provided.

The low cost imperative for NFPs in the age services sector is difficult enough in a financial environment where the prices paid by the NFP entity to for profit suppliers generally increase with CPI annually and wages and salaries must also keep pace with CPI. LASA Q sources only one seventh of its' income directly from members and to assist members financially, the Association limits annual membership fee increases to COPO instead of CPI.

The low cost imperative is of particular relevance in the age services NFP sector where a large proportion of the ageing population seeking residential and community care, housing and retirement living options have limited financial resources.

The removal of income tax concessions from the sector will reduce age service providers' ability to maintain low costs to clients.

The above issue is also sound grounds to retain income tax concessions with respect to competitive neutrality between the for profit and NFP sector.

In terms of the potential effects on competitive neutrality between NFP entities, some of which can access FBT concessions while others cannot, a more equitable application of eligibility criteria for access to concessions would be welcome, as LASA Q would see this as a step towards enabling greater participation in the age services sector.

In view of the tiered reporting approach taken by the ACNC, which is based on income thresholds, a tiered income tax concession approach based on taxable income, may provide a measure of compromise to spread the overall tax burden. However, the criteria for determining the tiers will be critical to ensure any changes minimise the real financial burden on the age services NFP sector.

Implementing a tiered approach will likely impose additional compliance burdens on entities that are currently exempt but will fall within the middle to large tiers. In many cases it is expected that these entities will incur additional costs and need support to develop the necessary skills to meet new compliance requirements.

It will also be critical to ensure any change to the tax regime with the intent to more equitably spread tax concessions, are followed with true income tax reductions in the greater population.

FBT Related Salary Benefits:

There is an issue for NFP age care services if they are unable to offer FBT related salary benefits. Already they are compromised in attracting staff vis-à-vis acute hospitals and other health and community service organisations where superior salary arrangements can be obtained. If FBT benefits were removed the current two tier system would be exacerbated.

It is policy that FBT salary packaging is offered to LASA Q employees only while the Association holds Public Benevolent Institution status. Currently the tax saving derived from providing packaging is retained by the Association. The Association has made it clear to all employees that in the event its' PBI status was removed, the Association would not be able to compensate individuals for the increased income tax that would be payable on the $16,050 currently received by employees as tax free.

The impact of losing income tax exemptions and the loss or reduction of existing FBT concessions will directly influence the capacity of LASA Q and other NFP entities in the age services sector to attract and retain qualified and committed staff within available resources.

While there is an additional administrative burden attached to offering salary packaging [LASA Q engages a service provider with individual employees paying the administration fee], the cost of this administration in direct payroll management time is estimated to be less than $5,000 per annum compared to the additional remuneration LASA Q would expect to have to pay to compensate employees for the tax saving foregone and State payroll tax implications may also apply.

The concerns over equity related to the FBT concessions for meals and entertainment are understandable, however, any change to remove access to these benefits will also have a significant impact on the NFP sector.

LASA Q's ability to attract and retain qualified staff within its' limited financial capacity is directly impacted by the opportunity to provide additional FBT related exemptions in relation to restaurant meals and entertainment facilities.

While high income professionals are able to access these benefits, LASA Q has evidence that its' employees on lower value salaries also access these benefits and the ability to do so has contributed to their decisions to accept employment.

LASA Q has experienced a significant staff turnover during the past 18 months with incoming employees finding the complexity of the FBT legislation and its' influence on the salary package offerings of the Association confusing, particularly when compared to their salary from previous employment in either the government or private sector. Understanding of the legislation is further complicated by its' interaction with other Government payments. While the FBT concessions are a critical factor for LASA Q to attract and retain employees, this complexity has made it difficult for employees to gain a true view of their remuneration at the point of engagement.

While bringing the meal and entertainment benefits to within the cap would appear to address the concerns over misuse of the concessions by high paid professionals, if the cap were kept at $16,050 the change would be an impediment to the recruitment of suitably qualified staff in terms of remuneration offers. If the major concern is regarding excessive use of the unlimited concessions, retaining the non-meal and entertainment concessions cap at $16,050 and placing a separate cap on these concessions would appear to be a suitable solution. To address the misuse issue, the setting of this separate cap at say, $10,000 would maximise the potential for employees in lower paid roles to utilise the concession, while ensuring higher paid individuals did not exceed reasonable benefits.

The 2012-13 changes to the income tax thresholds have also provided well received tax relief for LASA Q's lower paid employees. These employees saw a real value tax saving from the combination of the $18,000 tax free threshold and the non-grossed up $16,050 FBT value.

While the complexity of the legislation does not significantly add to the administrative burden of LASA Q, the flexibility available to employees in revising their packaging arrangements from payroll to payroll is a significant contributor. Any addition to this compliance activity, such as requiring concession declarations from individuals, would be onerous.

Despite its' complexity, LASA Q will not support the replacement of existing FBT concessions with alternative government support as outlined in Option 3.6, regardless of the model of support or with a tax offset system as outlined in Option 3.7.

As stated above, the cost of administration for a small entity such as LASA Q is far outweighed by the direct financial savings in being able to offer salary packaging to recruit and engage staff.

There is significant historical information and more recently, following the cessation of long standing funding arrangements in the NFP sector by the Queensland Government, real evidence of the uncertainty inherent in government funding.

There is also the very real risk that as the NFP sector grows, available government funding will be stretched thinner as applications increase, leading to a more inequitable situation. Retaining a concessional model and making the concessions available to more NFP entities, will contribute to the growth and longevity of the NFP sector, rather than restricting it through government imposed financial constraints.

LASA Q disagrees with the statement that the refundable tax offset option in the Discussion Paper would eliminate significant compliance burdens, and be more transparent, equitable and simple, based on the feedback provided above.

The assumption that a one size fits all exemption amount payable per employee (particularly $2,800 based on an estimated $1.4 billion cost divided by an estimated 500,000 total employees) across the entire NFP sector is equitable is incorrect. Taking the LASA Q situation as a case in point, the Association is currently receiving an overall benefit much greater than this under current FBT concessions. Similarly, a direct tax offset to employees for a NFP entity such as LASA Q that currently retains the existing tax benefit, would result in a minimum increase in annual employee remuneration costs of approximately $175,000 ($5,000 per annum for 35 employees). These costs would either have to be passed on to LASA Q's clients (members, students and funders) which is likely to have the effect of further reducing the Association's income as clients withdraw requests for services or LASA Q would need to seek savings through efficiencies, which would limit its' capacity to deliver necessary services.

As a relatively small, under resourced NFP entity, the LASA Q example is pertinent in estimating the likely impact of withdrawing the existing FBT concessions.

Furthermore, in light of the concerns over misuse of uncapped meal and entertainment benefits by highly paid professionals, it would seem redundant to replace the existing concessions with a tax free allowance system that favours those same employees.

Option 3.8 of the Discussion Paper proposes limiting concessions to benefits incidental to employment. This option would effectively remove the greatest incentive to employment that the NFP sector can offer to attract and recruit suitably skilled employees. As mentioned previously, LASA Q represents many NFP providers in regional, rural and remote centres where retaining the existing tax benefits and the ability to effectively match the after tax income, through the provision of salary packaging of for profit entities, is critical to continued operation.

While LASA Q concedes there are inequities and unnecessary complexity and compliance burdens attached to the current FBT concessional model, LASA Q trusts that the above commentary sufficiently illustrates the importance of these concessions in terms of the financial sustainability of the NFP age services sector.

Budget Neutral Reform:

There is significant risk in assuming the budget neutrality of the proposed options in the Discussion Paper will not have a detrimental impact on the NFP sector. The budget neutrality is offered in terms of the impact on the total population through changes to the taxation regime.

The larger impact on the NFP sector has not been addressed in the Discussion Pper, specifically the impacts at the entity level. Some NFP entities would definitely see gains through extension of the DGR scheme, however, others would be impacted negatively through employee recruitment and retention losses if existing FBT concessions were withdrawn. LASA Q would support a more comprehensive analysis of the likely impacts, both financial and in terms of service delivery, of the reform options.