Australian Catholic Bishops Conference

Response to the Discussion Paper "Fairer, simpler and more effective tax concessions for the not-for-profit sector"

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INTRODUCTION

The purpose of the Catholic Church in Australia and its agencies (the Church) is to contribute in a wide variety of ways across the spectrum of Australian society. As an integral part of its core mission, the Church seeks to assist people experience the fullness of life. It is concerned with all that impacts on human wellbeing. It comprises many thousands of different entities which have different purposes, modes of governance, and are subject to varying types and levels of government regulation.

The Australian Catholic Bishops Conference (ACBC) is a permanent institution of the Catholic Church in Australia and the instrumentality used by the Australian Catholic Bishops to act nationally and address issues of national significance. This submission has been drafted in consultation with the National Catholic Education Commission (NCEC).

The Church has engaged with government at each point in the reform process and this submission is made in that context. We appreciate the opportunity to participate.

Catholic Health Australia (CHA) and Catholic Social Services Australia (CSSA) will make separate representations on any issues in the Discussion Paper relating specifically to their sector. The ACBC supports submissions contributed by CHA and CSSA.

Catholic Church Structure

There are currently 3,663 entities in the Catholic Church Goods and Services Tax (GST) religious group. This does not reflect all the entities that comprise the Church as in many cases all the Catholic schools in a diocese were endorsed as one entity and in other cases entities were endorsed as branches. The Catholic Church comprises parishes, organisations within parishes, dioceses, religious orders, provinces, the church nationally and local entities that are part of the church internationally. Generally, members of the Catholic Church belong to a parish and are called parishioners.

Parishioners provide non tax-deductible contributions (e.g. deposited voluntarily to collections before, during and after church services) and tax-deductible contributions (e.g. donations to registered school building funds). Donors, unlike shareholders in a public company or depositors or investors with a financial institution, neither receive nor expect a *private* financial return on their contributions to Church activities which include many and varied works by big and small, metropolitan and provincial and remote rural parishes and parish entities. Therefore, the concept of risk may take on a completely different character for a donor than for an investor. However, it is recognised that both donors and investors are equally interested in transparency.

Parishioners identify with the community benefit and social capital generated by their local parish and church activities. They are able to observe directly how their contribution is applied locally through their direct involvement in worship and other parish activities. The status of donor is entirely different to say a shareholder in a public company, or a depositor in a financial institution who desires not only to know how revenues and profits are allocated, but also the prospect of a return on their financial investment.

EXECUTIVE SUMMARY

In this submission, the ACBC addresses a number of over-arching general issues that the Working Group may wish to consider in addition to specific responses to questions raised in the Working Group's Discussion Paper.

The ACBC noted the framework of budget neutrality in which the Working Group was asked to prepare advice. The ACBC is of the view that the Government should consider budget neutrality from a long-term and not a short-term perspective. The ways in which the Government might broaden the tax base for some NFPs would take several years to introduce. But sensible simplification of the tax arrangements for charities should be tackled expeditiously as good tax policy even if such action is at a short-term cost to the Budget.

This Executive Summary concludes with a summary of the recommendations on general issues, the specific issues best understood in the context of the questions as raised.

RECOMMENDATIONS – GENERAL ISSUES

The ACBC recommends that the Working Group seriously consider the following propositions set out in relation to particular issues for feedback raised in the Discussion Paper.

1. tax reforms applicable to charities, reforms to the entire NFP sector and reforms more appropriate to those NFPs which are not charities need to be clearly distinguished;
2. within any budget-neutral treatment of the NFP sector as a whole, a lower tax burden and simpler collection for charities should be policy priorities;
3. any broadening of the tax bases for charities by removal of concessions or inclusion of factors currently not taxed should be accompanied by a lowering of tax rates or raising of tax-free thresholds in preference to any new programs of grants;
4. the Commonwealth should work with the States to ensure that budget neutral strategies at the Commonwealth level for charities do not lead to adverse fiscal responses by State Governments; and
5. the timing of any reforms to tax concessions should have regard to the very significant change currently occurring across the charitable sector with the introduction of the Australian Charities and Not-for-profits Commission.

DETAILED COMMENTS

1. ACBC recommendation: *tax reforms applicable to charities, reforms to the entire NFP sector and reforms more appropriate to those NFPs which are not charities need to be clearly distinguished.*

The Discussion Paper ranges in its focus from technical issues such as the threshold for deductible gifts (currently $2) for charities to the widespread practice of gaming clubs signing patrons as members to ensure compliance with income tax laws. While it is not the Working Group's task to advise on government priorities for policy – there is a good case for distinguishing measures that will impact on the efficiency of operations for charities from measures to better align the tax base for other NFPs (e g sporting clubs) with the intent of existing taxation law. Sporting clubs may have broader public benefits, but primarily their activities centre on the preferences of paid-up members, many of whom are willing and have the capacity to pay membership fees. On the other hand, charities by and large serve targeted or general communities of people with disadvantage or disability and who have little ability to contribute financially to the cost of the services provided to them.

2. ACBC recommendation: *within any budget-neutral treatment of the NFP sector as a whole, a lower tax burden and simpler collection for charities should be policy priorities*.

Whether or not the Government wishes tax measures to be revenue-neutral across the NFP sector, an additional goal should be to introduce simpler more effective tax treatment of charities in such a way that, as far as practicable, no charity (and hence no clients with disadvantage or disability) is worse off after the tax reforms. It is important that charities and their clients do not have a needless source of uncertainty at a time when services for many charities serving the needs of the poor, disabled and mentally ill for example are stretched to meet demand. The ACBC also notes that given the discussion paper notes the value of tax concessions "... cannot be reliably estimated ..." (paragraph 4), it will be very difficult to provide reliable evidence of budget neutrality.

3. ACBC recommendation: *any broadening of the tax bases for charities by removal of concessions or inclusion of factors currently not taxed should be accompanied by a lowering of tax rates or raising of tax-free thresholds in preference to any new programs of grants*.

In *theory*, replacement of a tax concession by an accountable specific grant will have some advantages in terms of fiscal efficiency and accountability. But in *practice* this argument needs to be placed against the likely consequences of going down this path. Administration of grants has the potential to add red tape. In the case of charities, the sector is already subject to an increasing trend in contracting of services and a plethora of funding programs for pilots with uncertain futures. To add to government expenditures at the expense of tax concessions now would of necessity add to financial uncertainty and quite possibly the net regulatory burden[1] for charities.

4. ACBC recommendation: *the Government should work with the States to ensure that budget neutral strategies at the Commonwealth level for charities do not lead to adverse fiscal responses by State Governments.*

The ACBC would be concerned as would the charities sector more broadly if the condition of budget neutrality at the Commonwealth level for charities was achieved at the expense of measures that impacted on service delivery or funding at the level of State Government. For example, if the funding of Commonwealth action on tax concessions was met by reductions in Commonwealth contributions to programs requiring matching grants from the States, the net outcome overall might be negative for the sector. The Government needs to take into account the entire fiscal impact of charities including likely State, Territory and local Government responses. It is important therefore that the Commonwealth work closely with State Governments in reform of NFP tax concessions.

5. ACBC recommendation: *the timing of any reforms to tax concessions should have regard to the very significant change currently occurring across the charitable sector with the introduction of the Australian Charities and Not-for-profits Commission.*

The rapid rate of reform with the recent establishment of the Australian Charities and Not-for-Profits Commission (ACNC) makes the ability of the NFP sector to cope with further reform in such a short timeframe excessive, especially when many facets of the operations of the ACNC are yet to be addressed, such as financial reporting and governance requirements.

The ACBC recommends that the Working Group seriously consider the following comments set out in relation to particular issues for feedback raised in the Discussion Paper.

[1] Some concessions involve red tape (e.g. $2 threshold for tax deductible donations) but new grant schemes will almost certainly involve new red tape – even with the regulatory efficiencies expected to result from the operation of the ACNC.

SPECIFIC QUESTIONS RAISED IN THE DISCUSSION PAPER

Income Tax Eligibility

> **Q 1 What criteria should be used to determine whether an entity is entitled to an income tax exemption?**
> **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?**
> **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?**
> **Q 4 Does the tax system create particular impediments for large or complex NFPs?**

ACBC Response:

The current regime of income tax exemptions should remain in place for charities. With the introduction of new classifications of charities in the ACNC Act, it is accepted that over time there may be attempts to align ATO categories and ACNC classifications. However, any such rationalising of categories should not change the tax position of individual charities.

Tax exemptions should continue to apply to charitable entities, including religious entities, based on their accepted public benefit and encouragement of benevolent activities. The rationale for tax exemption for religious entities is the same as the rationale for tax exemption as other charitable bodies – religious entities pursue charitable purposes which, by definition, are for the public benefit.

Franking credits

> **Q 5 Should other types of NFPs also be able to claim a refund of franking credits?**
> **Q 6 Should the ability of tax exempt charities and DGRs to receive refunds for franking credits be limited?**

ACBC Response:

The ACBC is of the view that the current arrangements do not require any change. Moreover, with the challenges confronting the sector in relation to governance and compliance with the new national framework for regulation of charities, it would not be wise to subject charities to the need to review and revamp their investment strategies in light of changed arrangements with franking credits. Some entities within the Church place considerable store on franking credits received in relation to prudent investment of entity funds for a given purpose.

ATO endorsement

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

ACBC Response: this option is worth considering in conjunction with extension of the regulatory reach of the ACNC to NFPs other than charities after 1 July 2014 if it can be shown it will reduce red tape for the sector.

ITAA rationalisation

> **Q 8 Should the income tax exemptions for State, Territory and local government bodies be simplified and consolidated into the ITAA 1997? Which entities should be included?**

ACBC Response:

Simplification and consolidation of tax exemptions for State and Territory bodies may have merit, but not at the expense of increased vertical fiscal imbalance.

All State and Territory Governments are dependent on Commonwealth Government grants to fund their activities. If the States and Territories lose their tax exempt status the Commonwealth would collect more revenue but would, in turn, have to distribute more revenue to support State and Territory expenditure.

Income tax returns

> **Q 9 Should the threshold for income tax exemptions for taxable NFP clubs, associations and societies is increased? What would a suitable level be for an updated threshold?**

ACBC Response:

No comment.

General

> **Q 10 Please outlines 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.**

ACBC Response

The Government should consider development of target rates for red tape reduction, including the ‘principle of simplicity’ and reform of tax concessions, so that they are measurable and transparent and costed to ensure budget-neutral positions for NFP entities.

DGR status

> **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?**
>
> **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?**
>
> **Q 13 Would DGR endorsement at the entity level with restrictions based on activity address the behavioural distortions in Australia's DGR framework? Could unintended consequences follow from this approach?**
>
> **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?**

ACBC Response

While the Catholic Church is not looking to broaden the range of Church entities in receipt of Deductible Gift Recipient (DGR) status at this point in time, we would not wish to see limits placed on the current DGR status of existing Church entities.

The Catholic Church will however review its position on eligibility for DGR status in the event that the Government introduces a statutory definition of charity.

The sectors in which Catholic entities work can ill afford uncertainty for either donors or charities relying upon donations benefitting from DGR status. Those Church entities that seek to become fully registered charities for advancement of religion, charitable child care services and primary and secondary Catholic schools offer a public benefit and should be eligible to apply for DGR status.

In the education sector, recent significant reviews and upcoming reforms in the non-government school sector are very challenging. Therefore, the ACBC and the NCEC would be greatly concerned about further changes to DGRs in that sector, as this has an impact on the ability of Catholic schools to meet specific needs such as school building. These all derive from parents and other Parish contributions from their limited disposable income and the current economic climate. This is even more of importance with the present lack of certainty with future capital funding to schools and the provision of new schools. Factors such as attracting teachers and leaders to the non-government education sector are influenced by the current tax concessions and salary packaging options available as funding resources (including government and private income) of Catholic schools are on average less than government schools.

The ACBC and NCEC have no difficulty with an equitable application of DGR status across all education sectors including government schools. There are already strict requirements in place that work well including funding agreements to ensure that DGR donations are of a voluntary nature and school based income of all sources is appropriately utilised.

The ACBC and NCEC support in principle the Gonski recommendation outlined in paragraph 76 of the Discussion Paper that "…. (Gonski Review) *recommended that the Australian Government create a fund to provide national leadership in philanthropy in schooling, and to support schools in need of assistance including by providing schools with funding for buildings or scholarships. The Gonski Review recommends that the fund should operate under DGR status and that donors should be able to influence where funds are directed. The Government has initiated a separate process to respond to the recommendations in the Gonski Review, including the recommendation to set up a philanthropic fund*."

ACBC and NCEC reserve further comment on the Gonski recommendations until further details are released.

Tax Offsets to Replace Tax Deductions for Giving

> **Q 15 Would a fixed tax offset deliver fairer outcomes? Would a fixed tax offset be more complex than the current system? Would a fixed tax offset be as effective as the current system in terms of recognising giving?**
>
> **Q 16 Would having a two tiered tax offset encourage giving by higher income earners?**
>
> **Q 17 What other strategies would encourage giving to DGRs, especially by high income earners?**
>
> **Q 18 Should testamentary giving be encouraged through tax concessions and what mechanisms could be considered to address simplicity, integrity and effectiveness issues?**

ACBC Response

The Productivity Commission predicted that a fixed tax offset would result in a small overall decline in the level of giving to DGRs (see Discussion Paper at paragraph 92). Based on that evidence, the introduction of a fixed tax offset is contrary to the stated goal of increasing donations. If a fixed tax offset rate was used, e.g. such as the existing 20% tax offset over threshold for net medical expenses, and this rate was to be lower than the marginal tax rate of low, middle and/or high income individuals this would clearly be detrimental to donors and have a deleterious impact on donations, which would be contrary to the stated objective of increasing donations, especially from high income earners.

The ACNC should be tasked with the responsibility to encourage giving to DGRs, especially by high income earners.

The current rules on testamentary gifts are appropriate. It is difficult to conceive of reforms which would be fair and efficient.

Giving: clearing house / workplace giving

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

ACBC Response

Catholic charities have traditionally raised funds through the development of relationships within local communities and parishes and with donors committed to the mission and vision of the charity. There is a diversity of these arrangements across the charities sector. The ACBC does not see a role for the ACNC in the conduct of this fundraising, and therefore does not support the concept of the ACNC acting as a clearing house for the sector in relation to fundraising.

Corporate donations and donations of property

> **Q 21 Do valuation requirements and costs restrict the donation of property? What could be done to improve the requirements?**
>
> **Q 22 Is there a need to review and simplify the integrity rules?**
>
> **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?**

ACBC Response

Simplification of regulatory compliance related to corporate donations is worth a detailed review. Reform which simplifies the valuation rules would be welcomed. The ACBC reserves any detailed comments until the design of simplification proposals is known.

Public fund requirements

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

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

ACBC Response

Elimination of the public fund requirement is an opportunity to reduce red tape. It appears that registration of charities with the ACNC and the associated oversight of governance and financial reporting will supersede the need for the ATO to scrutinise public fund requirements.

Deductible gift threshold

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

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.

ACBC Response

Raising the threshold for deductible gifts to $10 is supported among measures to reduce red tape for the sector and donors. The measure would have greater merit if combined with the introduction of tax offsets in place of tax deductions as the impact on low income earners with limited capacity to give would be reduced.

Fringe Benefits Tax (FBT)

ACBC General Comments on Qns 28-42

The ACBC is of the view that the community benefits generated by the current arrangements with fringe benefit taxation and related concessions far outweigh the costs on economic efficiency and fiscal grounds.

While some streamlining might be desirable, the Government should ensure that any measures do not diminish the level of concessions available to employees engaged in the delivery of education, health and social services.

The ACBC supports the positions submitted by CHA and CSSA on these issues.

The ACBC reserves the right to comment to the working party if the removal of FBT concessions is tabled in future.

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?

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?

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?

ACBC Response

While fringe benefits tax arrangements have become entrenched in labour markets for workers in health and charities more generally, the reality is that the availability of skilled resources in these sectors are under considerable stress. When considering reforms to fringe benefit concessions, it is critical that the Government take no measures that will jeopardise the supply of skilled labour in these sectors.

The current exemption for fringe benefits in relation to live-in employees of religious institutions should be retained.

In relation to other technical detail relating to fringe benefits taxation, the ACBC supports the more detailed submissions by CHA and CSSA.

Meal and entertainment allowances

Q 31 Should salary sacrificed meal entertainment and entertainment facility leasing benefits be brought within the existing caps on FBT concessions?

Q 32 Should the caps for FBT concessions be increased if meal entertainment and entertainment facility leasing benefits are brought within the caps? Should there be a separate cap for meal entertainment and entertainment facility leasing benefits? If so, what would be an appropriate amount for such a cap?

Q 33 Are there any types of meal entertainment or entertainment facility leasing benefits that should remain exempt/rebateable if these items are otherwise subject to the relevant caps?

ACBC Response

While the ACBC recognises the fiscal burden of these arrangements for the Government, the detail of any proposal will be critical to sector support. The ACBC supports the CHA and CSSA submissions on these matters.

FBT with multiple employers

> **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?**

ACBC Response

In the interests of achieving horizontal equity, the number of employers an employee has should not be a determining factor in the extent to which eligible employees can avail themselves of FBT concessions. However government action to address this anomaly should not have adverse consequences for the market for scarce skilled labour in the health and welfare sectors.

FBT rate alignment

> **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?**

ACBC Response

FBT rebates and FBT tax rates should be aligned in any reforms in this area of taxation.

Minor benefits exemption

> **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?**

ACBC Response

The ACBC supports removal of the limitation of the minor benefits exemption to tax exempt bodies.

FBT Concessions – possible phase-out

> **Q 37 Is the provision of FBT concessions to current eligible entities appropriate? Should the concessions be available to more NFP entities?**
>
> **Q 38 Should FBT concessions (that is, the exemption and rebate) be phased out?**
>
> **Q 39 Should FBT concessions be replaced with direct support for entities that benefit from the application of these concessions?**

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?

ACBC Response

The ACBC reserves the right to comment if any detailed plans are released.

FBT concessions –restricted to non-remuneration benefits

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

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?

ACBC Response

No comment.

Goods and Services Tax (GST)

Q 43 Does the existing fundraising 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?

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?

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

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

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?

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

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

ACBC Response

The ACBC does not have any particular difficulty with the operation of GST– but compliance is complicated. A principle-based definition of the types of fundraising activities that are input taxed to reduce the compliance burden for entities that engage in fundraising is recommended. Given the small amounts of revenue involved, revenue efficiency and regulatory efficiency need to be balanced.

The ACBC reserves the right to comment on specific detail of any proposed reforms in this area.

Mutuality / clubs (Discussion Paper Qns 50 – 55)

> **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?**
>
> **Q 51 What would be a suitable threshold and rate of tax if such activities were to be subject to tax?**
>
> **Q 52 Should the mutuality principle be extended to all NFP member-based organisations?**
>
> **Q 53 Should the mutuality principle be legislated to provide that all income from dealings between entities and their members is assessable?**
>
> **Q 54 Should a balancing adjustment be allowed for mutual clubs and societies to allow for mutual gains or mutual losses?**
>
> **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?**

ACBC Comment:

No comment

Next Steps

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

ACBC Comment:

No comment.

> **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? Is there**

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

ACBC Comment:

It has come to the ACBC's attention that there remains considerable concern across school administrations in relation to the income derived from "minor or occasional" use of school buildings and the effect the application of Tax Ruling TR 2011/D5 may have on school administrations. The ACBC encourages the ATO to keep the new ruling under review and be responsive to responsible representations for the school administrations in relation to this issue.