Mission Australia's response to the

Not-for-profit Sector Tax Concession Working Group Discussion Paper -

Fairer, simpler and more effective tax concessions for the not-for-profit sector

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Mission Australia

Mission Australia is a national, not for profit organisation that has been transforming the lives of Australians in need for more than 150 years. Our vision is to see a fairer Australia by enabling people in need to find pathways to a better life. The breadth and diversity of our programs reflects that vision – from early learning and youth services, extensive family support and homelessness initiatives, employment and skills development, to the provision of affordable housing.

In 2011-12 our Community Services delivered 326 services (including 28 Early Learning Services), that assisted 110,389 individuals and 5,732 families. Our Employment Solutions offered ten programs that assisted 165,000 individuals and helped 15,850 people move into sustainable employment in that same period. MA Housing meanwhile began 2011-12 managing 1,071 dwellings and closed the year with 1,418 dwellings and a 91% tenant satisfaction rating[1].

We provide these services, either under contract to government, through programs funded by grants and donations, or via social enterprises. All our activities are ancillary to our charitable purpose in that they directly provide outcomes and services for our client groups and any surplus funds are directed to supporting our altruistic activities.

Our response to the discussion paper

Mission Australia supports the timely review of tax concessions for the not-for-profit (NFP) sector and the intent of the working group to develop 'fairer, simpler and more effective tax concessions for the not-for-profit sector'. In our view it is also important the valuable contribution of the NFP sector in effectively and efficiently delivering services that would otherwise be provided by government at greater cost to tax payers also be recognised. We endorse the principles provided for in the Working Group's terms of reference that any proposed changes to tax concessions be at no additional cost.

We have previously commented on the other tax measures in train such as better targeting NFP tax concessions and the introduction of a statutory definition of charity. Although we have some concerns about aspects of these reforms we believe a statutory definition of charity which codifies existing case law as well as capturing contemporary charitable practice such as early intervention, social enterprise and social and affordable housing programs is timely. We also supported the in-principle intention behind the Assistant Treasurer's announcement that taxation support provided to the NFP sector is targeted to supporting the altruistic activities of the sector and not directed to supporting unrelated commercial activities but cautioned that legitimate commercial activity ancillary to the primary purpose of a charity should not become liable to taxation as a result of any unintended consequences of the proposed legislation.

Further we have commented on other aspects of sector reform including being supportive of the establishment of a national NFP regulator; we also commented specifically on the development of the ACNC and associated legislative proposals. In those responses we also expressed our view that the emphasis for a national regulator should be on strengthening and supporting the sector, reducing current compliance and regulatory burdens (such as improving transparency and removing red tape) and public education.

[1] Our 2012 Annual Report is be available for download from http://www.missionpromotion.com/annualreport/

In terms of our response to the *Not-for-profit Sector Tax Concession Working Group Discussion Paper we* have restricted our responses to those chapters and questions directly relevant to our experience and our concession status - we are a public benevolent institution. Our key points for the Working Group's consideration are outlined below and specific responses to the questions posed are provided in the next section.

Key points

Mission Australia would wish to see alignment of this review of tax concessions with the broader agenda associated with the NFP sector such as those outlined above – definition of charity, national regulator and so on. In our view this alignment will help to achieve:

- *Simplification*
  Understanding and navigating the tax and other related systems can be complicated for both NFPs and their donors. Mission Australia is keen to see simplification of these systems (particularly those around FBT) as a means to reduce administrative burden so that NFPs like ours can focus on the delivery of effective and efficient services rather than allocate scarce staffing resources away from the delivery of those services to comply with overly complex requirements.

  We would also be keen to see processes simplified to make it easier for donors to make their donations as and how they choose to, so simplifying processes and making tax implications clearer should help donors better understand how they can maximise their donation.

- *Accessibility*
  We support the development of processes and systems to better assist donors to navigate both the volume and breadth of NFPs in the sector as provided for in the ACNC portal. An easier and more transparent way to determine the NFP's entity and purpose, their concession status and similar information could improve accessibility for donors generally. This combined with more simplicity in terms of making donations (as highlighted above) could in turn encourage more donations – including through workplace giving.

- *Strengthening the NFP sector*
  Fairer, simpler and more effective tax concessions, in our view, will help to further develop the capacity within the sector by:
  - encouraging highly skilled individuals into the sector as the disparity in pay rates is addressed by better tax incentives;
  - fostering a climate whereby innovation in service delivery is encouraged and enabled as a result of less complex and onerous administration; and
  - formally acknowledging the valuable contribution of the NFP sector.

Chapter 1 – Income Tax Exemption and Refundable Franking Credits

Q1. What criteria should be used to determine whether an entity is entitled to an income tax exemption?

Mission Australia supports the current criteria for determining an entity's entitlement to both ordinary income and statutory income tax exemption – namely for public benefit and charitable purpose.

Q2. 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?

In our view the current categories of income tax exempt entities are appropriate.

Q4. Does the tax system create particular impediments for large or complex NFPs?

Mission Australia is concerned that there are some potential impediments for large or complex NFPs such as our own. In our view we would like to see a focus of the tax system on the entire entity and purpose rather than a focus on an activity basis when determining exemptions not least of all because a focus on activity levels will create a lot of work for an organisation with the size and breadth of Mission Australia. Such an approach also encourages the development of sector depth, diversity and simplicity.

In summary:
Mission Australia supports a holistic focus on entity and purpose, rather than on individual activities, when determining exemptions.

Q5. Should other types of NFPs also be able to claim a refund of franking credits?

In our view there is a need to ensure that income received by a NFP remains tax exempt, no matter what the method of receipt is. We are also concerned that changes to an NFPs ability to claim a refund of franking credits may distort investment decisions, for example toward property or cash type investments which may not be in the best interests of the entity's purpose.

Q6. Should the ability of tax exempt charities and DGRs to receive refunds for franking credits be limited?

In our view the ability of tax exempt charities and DGRs to receive refunds for franking should not be limited as this ensures that all income received, regardless of the method of receipt, remains tax exempt. This approach also ensures there is simplicity and consistency and broad principles are advocated.

Q7. Should the ATO endorsement framework be extended to include NFP entities other than charities seeking tax exemption?

No, Mission Australia does not support the ATO endorsement framework being extended to include NFP entities other than charities seeking tax exemption. In our view this is against the principle of reducing compliance for the NFP sector, therefore only DGRs should go through the endorsement framework as their tax exemptions are much higher.

General

Q10. 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.

Mission Australia supports fundraising methods which facilitate delivering pre-tax income as donations rather than as post-tax funds. This would enable wider tax deductibility. For example, people who give through an offering plate or 'bucket' donation are donating from post-tax funds and therefore don't receive a deduction. In our view there is a need to simplify the ways in which these types of collections are made so they have the same impact as if they were given from pre-tax funds. For example, the UK "Gift Aid" model[2] would be our recommended method of application and would help to improve the fairness, simplicity and effectiveness of the income tax exemption regime.

Australian charities follow a fee-dominant model that is 63% of funds are privately raised[3]. While the market in Australia for NFP services is large, further growth is limited because of the dependence on private fundraising. As only about 30% of fundraising in Australia comes from government, with the remainder raised privately, further support by government will increase the NFP sector's efficiency and effectiveness.

Increasing the available range of deductible gifts is an excellent way of providing such support. Gifts to charities have been deductible in Australia since the introduction of Commonwealth income tax legislation in 1915[4]. In 2008-2009, individual taxpayers claimed $31.67 billion in tax deductions, of which only 6.61% were for tax deductible gifts, valued at $2.09 billion[5]. (Corporate giving is not included in those figures because ATO does not keep those statistics).

Treasury has estimated that the cost of providing gift deductibility was $710 million in 2007-2008[6]. These figures indicate that the cost of tax deductible donations is low compared to their value to the charities that benefit from them. Given the small cost of gift deductibility compared to the productivity of the NFP sector, there is no good economic reason to reduce this level of subsidy; or to waive or restrict tax deductibility of donations; or reduce the number of DGRs. Rather there is a solid argument for government support to be increased for a sector which is so valuable to the Australian community, both economically and socially.

Rather than removing or restricting tax exemptions for NFPs, Treasury should define its priorities for tax collection while encouraging fundraising methods which facilitate donations from pre-tax income.

In summary:

Fundraising methods to facilitate donations from pre-tax income should be encouraged as they will assist charities with developing a secure income stream at low cost.

[2] More information about the Gift Aid model is available at http://www.hmrc.gov.uk/individuals/giving/gift-aid.htm
[3] Salamon & Anheir, (1999) *The Emerging Sector Revisited,* Baltimore, Centre for Civil Society Studies, Institute for Policy Studies, Johns Hopkins University.
[4] O'Connell (2008) *The Tax Position of Charities in Australia – why does it have to be so complicated.* ATRev 17 at 21
[5] M. McGregor-Lowndes and E. Pelling, *An examination of tax deductible donations made by individual Australian taxpayers in 2008-09*, May 2011, The Australian Centre for Philanthropy and Nonprofit Studies, Queensland University of Technology)
[6] O'Connell, citing *Treasury, Tax Expenditure Statement 2006*, item A64).

Chapter 2 – Deductible Gift Recipients

Q11. 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?

As noted above, Mission Australia would wish to see a more equitable DGR system for all charities to enable gifts to be made pre rather than post tax. Currently the exclusion of deductibility for gifts to primary and secondary schools, for example, acts as a disincentive to support under-funded education programs and initiatives that make a valuable contribution to society in preventing longer-term social problems. Mission Australia would therefore support the extension of DGR status to all charities over time, as recommended by the Productivity Commission. We acknowledge that such a move would incur a cost to revenue but this could be offset by limiting FBT and other uncapped benefits currently available to NFP employees.

Q13. 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?

The discussion paper has not identified any behavioural distortions in Australia's DGR framework. Mission Australia cautions against limiting the activities a DGR is allowed to conduct in pursuance of its charitable purpose. In a rapidly and continuously changing economic environment, this may cause a DGR such as Mission Australia to miss a valuable opportunity to raise funds for its purpose. As the High Court of Australia recognised in *Commissioner of Taxation v Word Investments Ltd*[7], it is for the public benefit that DGRs engage in practical activities to raise funds in pursuance of their purpose, rather than relying solely on donations or other passive forms of fundraising such as bequests**.**

In our view entity level endorsement with restrictions based on activity could result in significantly increased complexity for large NFPs like Mission Australia (as per Q4). For example, under this proposal we could be restricted from using donations made by individuals/philanthropists for our chaplaincy and early learning services. This is particularly problematic as many of the early learning centres we operate are in low socio-economic areas and operate at or below a break-even level. The significant community benefits associated with the provision of child care in these lower socio-economic areas, which are consistent with our organisational purpose would therefore be reduced.

In summary:
DGR endorsement should relate to an entity's purpose, rather than the activities it carries out.

Q15. 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?

We would be concerned that any move to a fixed tax offset system would act as a disincentive for those on higher tax rates to give. Mission Australia are of the view that the current tax deduction system is well understood, so if there is an intention to move to a tax offset system, there would need to be an extensive public education program to help potential donors understand impact it would have on them. Such a program would only divert scarce organisational and government funds from service delivery.

[7] *Commissioner of Taxation v Word Investments Ltd* [2008] HCA 55

Should the government proceed with a tax offset system, Mission Australia would like any changes to the tax offset to encourage more people to donate by offering tax offset rates above other expenses and claims. The amounts would also need to reflect changes in marginal tax rates should they be provided. In our view, one way of fixed offsets delivering fairer outcomes is to ensure the offset does not impact people by providing a lower offset than they can claim through other expenses, for example if someone claims 34% tax offset through donations under $1000 but can claim 45% through other expenses there is less inclination to donate.

In summary:
Mission Australia supports the status quo.

Q16. Would having a two tiered tax offset encourage giving by higher income earners?

Further to our response to Question 15, the rates proposed in the discussion paper could act as a disincentive for those on higher tax rates to make donations to the NFP sector.

Q17. What other strategies would encourage giving to DGRs, especially by high income earners?

Mission Australia considers that existing deduction arrangements should be kept in place for PAFs. PAFs are a relatively new vehicle for facilitating philanthropic giving and given the changes from the old PPFs and the impact of the global financial crisis, any further changes risk damaging confidence in philanthropy at a time when these vehicles need to be encouraged.

Q18. Should testamentary giving be encouraged through tax concessions and what mechanisms could be considered to address simplicity, integrity and effectiveness issues?

In Australia, there are no death duties on estates and for this reason it is difficult to see what value there would be to an estate in claiming a tax deduction for a testamentary gift. A possible exception would be to minimise capital tax gains on property bequests valued over $5,000. For this reason, Mission Australia supports the continuation of Capital Gains Tax exemptions for donations made via testamentary gifts. It is our opinion that the method proposed by the Mitchell Review (outlined at paragraph 100) provides too much complexity and possibility for avoidance.

Q19. Would a clearing house linked to the ACNC Register be beneficial for the sector and public?

Mission Australia would support in principle the development of a clearing house for a number of reasons including: the tax pre-fill option will help to reduce administrative burden and enables electronic receipting; it will be easier to evidence tax deductibility; and allows for the pre-population of e-tax.

We have concerns however about a clearing house proposal, not least of all those relating to the estimated once-off capital cost of around $25 million. It is also unclear whether or not there will be administration costs charged for inclusion on and use of the clearing house. There is also the potential for organisations, including our own, to experience a loss of identity particularly in relation to ongoing communication to donors and the increased distance of the interface between us and our donors. It is unclear to us how the proposed clearing house would dovetail into organisations existing online strategies so we would appreciate some clarity around the relationship between the clearing house and registered entities existing online presence – including that for online fundraising facilities.

In our view more detail is required about the specifics of how a clearing house linked to the ACNC Register might operate so that NFPs are better able to determine the merits or otherwise of the suggested approach.

In summary:
Mission Australia supports, in principle, the development of a clearing house linked to the ACNC register but would want the capacity for DGRs to be able to continue to communicate directly with donors.

Q20. 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?

Mission Australia supports further consultation for proposals to simplify regular donations by larger numbers of people, including the wider adoption of workplace giving programs. In our experience having total donations pre-filled on PAYG Payment Summaries assists to reduce any administrative burden.

Q21. Do valuation requirements and costs restrict the donation of property? What could be done to improve the requirements?

In our view the current rules are complex and do not allow for easy transfer of goods or services. Gifts of property that fall outside of the 12 months / $5000 rules in particular require valuation by ATO, and are done at the cost of the donor. A donor may be discouraged as the cost of the valuation is non-deductible and non-refundable if it is determined the item has limited value. Further, the charity receiving the donation is unable to reimburse the costs of obtaining the valuation to the donor and this creates a barrier to recognising donations.

Our view is that the following changes to the existing system would enable simplification:

- that the process is made as simple and as transparent as possible;
- that the associated fees are made tax deductible to the donor so long as these charges are not passed on to the charity;
- a SLA on the delivery of the valuation is put in place so that both the donor and NFP know when valuation documents are expected; and
- the $5000 limit is indexed

Q22. Is there a need to review and simplify the integrity rules?

Mission Australia's experience is that, while the integrity rules are important to maintain, the current complexity of these rules limits the donations available to DGRs and requires simplification as per the changes proposed above in response to Q21.

Q23. 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?

There are two needs which Mission Australia has identified:

1. There is no mechanism for companies to claim a deduction for items sold to DGRs at a discounted price. For example, if trading stock is provided for free then a deduction for the value of goods donated can be claimed, however if trading stock is provided below cost a deduction is not available. The difficulties in valuing a genuine deduction would make this difficult to implement (for example, would a "government rate" that is essentially a discount that applies for charities count as a donation?). It may be possible to determine a fixed percentage of retail price in order to reduce the administrative burden.

2. There are no deductions available for professional services firms who donate their time to provide professional assistance to DGRs. In our view, a suitable way to distinguish this donated time from volunteering activity would be where advice provided/work completed is covered by professional indemnity insurance or any other similar cover. While valuation of time could be difficult it may be possible to determine at a fixed percentage of standard hourly rates in order to reduce the associated administrative burden.

In summary:

Mission Australia supports the following reforms:

1. Enable companies to claim a deduction for items sold to DGRs at a discounted price; and
2. Enable professional services firms who donate their time to provide professional assistance to DGRs to claim a tax deduction for the notional cost of those service

Q26. Should the threshold for deductible gifts be increased from $2 to $25 (or to some other amount)?

Although this was a recommendation of the Australia's Future Tax System review (Henry review), there are some concerns that increasing the threshold may not be advisable given the strong marketing message associated with the current deductible gift threshold and the potential negative impact on donations. Donations from $1-$50 remain a significant source of income to charities, as they enable low income earners to donate and all donors to make multiple donations[8]. Newer methods of fundraising such as face-to-face fundraising and workplace giving rely on high volume, low amount gifts to provide charities with a secure income stream. The Public Fundraising Regulatory Association (PFRA) estimate face-to-face fundraising raises £130million a year for UK charities, with a record 863,407 new donors signed up by PFRA members last year through street and door-to-door face-to-face fundraising methods. Averaging this, each donor is worth £150 per year or £12 per month[9].This strongly demonstrates the value to charities of high volume, low amount donations.

Further, if individuals can claim where they support multiple charities or make multiple donations with amounts under $25 this may reduce the risk of any detrimental impact associated with raising the threshold. There is a low administrative cost to charities associated with low amount donations

[8] M.McGregor-Lowndes & E. Pelling, op cit

[9] More information is available at http://www.institute-of-fundraising.org.uk/guidance/about-fundraising/face-to-face-activity/face-to-face-fundraising-the-facts-and-figures/

made through online portals or workplace giving because the costs of collection are passed to the collectors, not the charities.

In summary:

Mission Australia supports the existing tax deductible threshold of $2**.**

Q27. Outline any other suggestions you have to improve the fairness, simplicity and effectiveness of the DGR regime, having regard to the terms of reference.

Mission Australia supports the development of the social investment sector and therefore encourages measures that foster its growth. For example, Social Benefit Bonds are an emerging area for investment and assistance to the NFP sector, and as such we would seek that these emerging tools are given favourable tax treatment as they encourage the flow of capital into the sector which in turn lessens the relative pressure on government funding. Other suggestions we have are:

- that Government consider the NFP tax concession changes and regime in conjunction with the contemplations raised by the Productivity Commission process into the encouragement of Social Capital options for the NFP sector;
- the tax treatment of capital provided to the NFP sector is highly influential on both the cost and availability of this capital so should be carefully considered; and
- there is a need to discuss and consider the income tax treatment of interest/coupons as well as the treatment of CGT in loss scenarios.

In summary:

Mission Australia strongly supports the development of the social investment sector and therefore encourages any measures that foster its growth.

Chapter 3 – Fringe Benefits Tax Concessions

Q30. 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?

Mission Australia supports:

- the long term removal of the FBT Rebate/exemption rules and
- the introduction of a tax offset system for employees of eligible entities paid through regular earnings.

This option reduces the administrative burden for both employees and employers.

Q31. Should salary sacrificed meal entertainment and entertainment facility leasing benefits be brought within the existing caps on FBT concessions?

In our experience, these benefits are of much greater value to sector employees on higher incomes than they are to those on the lowest incomes. Mission Australia would therefore support including these benefits under the existing caps for FBT concessions. Further, in the interests of equity, we would support FBT concessions only being available to sector employees up to a salary cap of $120,000. Such changes to these benefits would need to be phased in so they do not act as a disincentive to attracting well qualified staff to the sector.

Q34. 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?

Mission Australia's experience is that compliance associated with FBT concessions is a difficult issue for charities such as ours, particularly given those who are eligible for multiple caps are likely to be low income earners who make limited use of the benefits. This issue could be addressed by employers when tax file number declaration forms are lodged at the commencement of employment

Q38. Should FBT concessions (that is, the exemption and rebate) be phased out?

The FBT concessions should be phased out over the long term for the following reasons:

- the current system is too complex;
- is of little benefit to part-time, low income employees; and
- the value of the $30,000 cap is being eroded by inflation and progressive increase in the tax free threshold.

However, any transition to an employee tax offset would need to be carefully managed so as not to make it more difficult for charities and NFPs to attract skilled staff. Mission Australia would support the current concessions being replaced by a simpler tax offset for employees.

Q39. Should FBT concessions be replaced with direct support for entities that benefit from the application of these concessions?

No. Mission Australia considers the benefit should be provided to the employee to better enable NFPs to attract staff to the sector. We note however, that the removal of FBT concessions would have unintended consequences regarding GST refunds currently available to our organisation as a result of salary packaging.

Q40. 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?

While Mission Australia supports a direct tax offset for employees of eligible entities through the PAYG system as this would allow assistance throughout the year, we are mindful of the need to accommodate HECS, Family tax benefit and other government benefits that may be deducted from employees' salaries.

Chapter 4 – Goods and Services Tax Concessions

Q44. 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 in our view, as allowing for self-assessment reduces the compliance burden for running these types of fundraising activities.

Q45. Should current GST concessions continue to apply for eligible NFP entities?

Yes.

Q46. Are there any other issues or concerns with the operation of the GST concessions in their current form?

The current operation of the GST concessions does pose some problems for Mission Australia. For example, the compliance issues regarding sale of goods is complex for our Big Heart store operations (one of our social enterprises). These retail stores currently sell a mix of donated second-hand goods (which are sold GST Free), goods purchased in bulk (i.e. not itemised and where purchase price compared to sale price is undetermined) and stock purchased and on-sold piece-meal (i.e. itemised).

In relation to bulk goods purchased, there is significant administrative time spent sorting through each item of clothing to determine the sale price and then determine if that sale price meets the requirement for GST-free status. For example, the bulk goods purchased or donated can be faulty stock or old stock (up to 3 years old). We are therefore required to first determine the value of the goods then determine if we are going to sell above or below 50% of market value. This is time consuming but also has minimal benefit given the sale price of most of these items are below $10 each.

Given the nature of the enterprise, most of the employees in our stores and warehouse are volunteers and require training around the importance of correctly tagging and then allocating sales in the appropriate GST categories. Given how complex the rules are, and the volunteer rather than skilled nature of the staff, compliance can be difficult. Ideally we could move to a more straightforward environment where the rules around sale of products that relate to "necessitous circumstances" would all be GST free, while commercial manufacturing operations (such as our recycling work in Featherweight, or other charity social enterprises with a jobs focus) are GST inclusive.

Should the current FBT system remain, we would support organisations such as our own continuing to have the benefits of the GST credits available through salary packaging. Should the FBT System be reformed, additional GST concessions should be considered to offset the amount.

Q49. Is there an alternative way of reducing the compliance burden associated with apportionment for supplies made for nominal consideration?

Further to our response to Q46, Mission Australia considers an exemption from GST may provide a means for reducing the compliance burden associated with the apportionment for supplies made for nominal consideration – as per the operational example provided. We would also like to see a reduction in the burden associated with calculating eligibility to claim input tax credits.