

## SUBMISSION TO THE TREASURY, *TAX DEDUCTIBLE GIFT RECIPIENT REFORM OPPORTUNITIES, DISCUSSION PAPER*

NOT-FOR-PROFIT PROJECT, UNIVERSITY OF MELBOURNE LAW SCHOOL

20 July 2017

### ABOUT THE NOT-FOR-PROFIT PROJECT

The University of Melbourne Law School's Not-for-profit Project (NFP Project) is a research project initially funded by the Australian Research Council. The NFP Project began in 2010 with the aim of providing a comprehensive legal analysis of the definition, taxation, and regulation of not-for-profit (NFP) organisations in Australia. [Appendix A](#) provides further information about the NFP Project and its members.

The NFP Project has been heavily engaged in the numerous consultation processes regarding reforms to the NFP sector since 2010. These earlier submissions are available at <http://law.unimelb.edu.au/centres/cclsr/research/major-research-projects/defining-taxing-and-regulating-the-not-for-profit-sector-in-australia-law-and-policy-for-the-21st-century>.

### SUMMARY OF OUR SUBMISSION

We agree with the general propositions in the Tax Deductible Gift Recipient Reform Opportunities Discussion Paper that:

- Deductible Gift Recipient (DGR) governance arrangements should be consistent, transparent and ensure accountability;
- Administrative complexity should be reduced; and
- Eligibility for tax concessions should be reviewed on a regular basis.

In relation to the issues raised in the Discussion Paper we recommend:

#### Recommendation 1:

All DGRs should be charities (as defined in the *Charities Act 2013*) or charitable-like government entities

#### Recommendation 2:

That there is no need for any additional requirements for environmental organisations in relation to advocacy further than those contained in the *Charities Act* and subject to the guidance on advocacy provided by the ACNC.

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### Recommendation 3:

The four registers in Div 30 of the *Income Tax Assessment Act 1997* (ITAA 1997) should be reviewed by the relevant departments and the Assistant Treasurer to see whether it is appropriate to transfer the entities on the registers to the Australian Charities and Not-for-profit Commission (ACNC) register and be subject to be endorsed by the Commissioner of Taxation. We agree that this is appropriate for the Register of Environmental Organisations.

### Recommendation 4:

That once entities are registered by the ACNC there is no compelling reason for maintaining the public fund requirement.

### Recommendation 5:

That the Australian Tax Office (ATO) should conduct regular reviews to determine whether entities are still eligible for DGR endorsement.

### Recommendation 6:

Specific listing should be removed with existing entities becoming registered charities (if appropriate) and being endorsed by the Commissioner of Taxation (if appropriate), subject to review of continuing eligibility

### Recommendation 7:

That Treasury give consideration to other issues related to the matters raised in the Discussion Paper to avoid inconsistencies and anomalies developing in the tax concessions for the not-for-profit (NFP) sector.

## 1. INTRODUCTION

The Treasury Discussion Paper outlines a number of proposals relating to DGR tax arrangements. The proposals are said to be aimed at:

- Strengthening DGR governance arrangements;
- Reducing administrative complexity; and
- Ensuring eligibility for the concessions is up to date.

The first of these matters could be described as being concerned with **consistency, transparency and accountability**, the second with **simplicity** and the third with **integrity**. We support these goals and welcome the opportunity to comment on issues raised in the Discussion Paper.

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Before addressing the issues and questions raised specifically in the Discussion Paper, we would like to address some comments made in previous reviews (Part 2 of this Submission); the historical development in Australia of the gift deduction (Part 3) the position in some other jurisdictions (Part 4) and the current position (Part 5). Following consideration of the matters raised in the Discussion Paper (Part 6) we would like to raise some additional matters for consideration (Part 7).

## 2. PREVIOUS REVIEWS

As noted in the Discussion Paper, there have been several reviews relating to the DGR provisions. The Report of the House of Representatives Standing Committee Inquiry into the Register of Environmental Organisations (REO Report) was quite targeted but raised the wider issue about the haphazard and inconsistent treatment of various entities under the DGR provisions. Importantly, the REO Report noted that ‘a broader and more thorough consideration of the entire DGR system by the Australian Government, in due course’.<sup>1</sup>

The possible reform of the DGR provisions was also considered as part of a wider review of tax concessions for the NFP sector by Treasury’s NFP Tax Concessions Working Group (TCWG) in 2012-2013 as also noted in the Discussion Paper. Several of the recommendations from the TCWG Report are similar to some of the proposals considered in the Discussion Paper. For example, the TCWG Report noted:

“The deductible gift recipient (DGR) framework is intended to encourage philanthropy. However, the current system for granting DGR status is cumbersome, inequitable and anomalous. Further, the framework is not well placed to handle organisations that carry out a range of purposes that fit within a number of DGR categories. Reforming the framework would increase certainty, reduce red tape for eligible entities and should further increase philanthropy.”<sup>2</sup>

It was recommended that:

“Entities that are currently specifically listed, or endorsed under existing DGR categories, should generally be required to seek registration as a charity to retain their DGR status. It is expected that the majority of current specifically listed or endorsed entities would fit within the proposed framework.”<sup>3</sup>

In addition it was recommended that:

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<sup>1</sup> House of Representatives Standing Committee Inquiry into the Register of Environmental Organisations Report April 2016, (REO Report) para 2.48.

<sup>2</sup> Treasury, Not-for-profit Sector Tax Concession Working Group: Fairer, Simpler and More Effective Tax Concessions for the Not-for-profit Sector, Final Report, May 2013, p 21:  
<https://www.treasury.gov.au/~media/Treasury/Access%20to%20Information/Disclosure%20Log/2014/1447/Downloads/PDF/NFP%20Sector%20WG%20Final%20Report.ashx>

<sup>3</sup> Ibid, Rec 6.5.

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“There should be a review of entities that are DGRs, but fall outside the accepted charitable purposes framework, to determine whether they still merit DGR status. This review would include:

- a. entities that are currently specifically listed as DGRs in Division 30 of the ITAA 1997 that will not qualify to be registered as charities; and
- b. DGR general categories that fall outside of existing charitable purposes.”<sup>4</sup>

The TCWG Report also recommended that there should be a separate DGR category for entities that would be charities but for their connection with government (such as public museums and art galleries).<sup>5</sup>

The TCWG Report also recommended extending the eligibility of entities in relation to DGR status.<sup>6</sup> It is noted that the Discussion Paper states that it is not concerned with extending eligibility but it is suggested that any review should at least note the arguments for extending eligibility in certain cases and the potential for simplification that could arise from that process.

In addition to the two reviews mentioned, the government has also announced, but so far not enacted, changes to the ‘in Australia’ requirements in both the DGR and income tax exemption provisions.<sup>7</sup>

The Australian National Audit Office (ANAO) also released a report on ‘Administration of Deductible Gift Recipients (Non-profit Sector)’ in June 2011.<sup>8</sup> The recommendations related to consistent decision-making of endorsement applications and the effectiveness of risk assessments. The ANAO report noted that despite limited resources, during 2009-10 the ATO completed 4 audits and 38 other reviews that resulted in 13 DGRs (32 percent) having their DGR status revoked.<sup>9</sup> The ANAO report also noted the distorting nature of the DGR provisions:

“...certain characteristics of the tax concession legislation create anomalies in the type of endorsement that organisations may apply for because some categories allow

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<sup>4</sup> Ibid, Rec 6.6.

<sup>5</sup> Ibid, Rec 5.4.

<sup>6</sup> Ibid, Rec 6.1.

<sup>7</sup> Treasury, Restating and Centralising the Special Conditions for Tax Concession Entities, Exposure Draft, March 2014: <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Conditions-for-tax-concession-entities>

<sup>8</sup> The Australian National Audit Office, Administration of Deductible Gift Recipients (Non-profit Sector) Report, June 2011: <https://www.anao.gov.au/work/performance-audit/administration-deductible-gift-recipients-non-profit-sector>

<sup>9</sup> Ibid, Summary, para 49.

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access to a broader range of tax concessions. As a consequence, organisations apply for status in categories that may not reflect the activities undertaken by them...”<sup>10</sup>

We also note that there have been reviews by the relevant departments in relation to the Guidelines relating to two of the Registers – Department of Foreign Affairs (DFAT) in 2015<sup>11</sup> and the Department of Social Services (DSS) updated its Guidelines in June 2017.<sup>12</sup>

### 3. HISTORICAL DEVELOPMENT

In order to fully understand why the existing DGR framework is in need of comprehensive reform it is useful to consider the historical development of Div 30 of the *Income Tax Assessment Act 1997*. The Discussion Paper outlines some of the historical developments that have led to the DGR regime being perceived as providing inconsistent treatment of entities, being overly complex and lacking integrity. The reasons why the current provisions are seen in this way includes the following:

- i. The general categories have been expanded in a fairly haphazard way without regard to any overarching policy principles.
- ii. Specific listing seems to have been an ad hoc reaction to certain entities possibly not falling within the general categories.
- iii. The four registers have developed at different times for quite different reasons.
- iv. The overall framework has not responded appropriately to significant developments, namely the introduction in 2001 of Private Ancillary Funds, the establishment of the Australian Charities and Not for Profits Commission in 2012, and the introduction of the statutory definition of charity in 2013.

#### (i) THE GENERAL CATEGORIES

The Discussion Paper notes the first Federal Income Tax Assessment Act in 1915 provided a deduction for certain gifts. The first tax deduction for gifts in Australia was contained in the *Income Tax Act 1907* (Vic). At the Commonwealth level, the provision as originally introduced only provided a deduction for gifts to a War Fund but was subsequently amended to include a deduction for 'gifts exceeding Twenty pounds each to public charitable institutions in Australia'.<sup>13</sup> In 1927 it was decided to reduce the minimum amount of the gift to one pound (and this has remained (\$2) as the minimum amount in all

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<sup>10</sup> Ibid, para 21. See also ATO Statistics in n 86.

<sup>11</sup> DFAT, Review of the Overseas Aid Gift Deduction Scheme, August 2015: <https://dfat.gov.au/about-us/publications/Documents/oagds-review-summary-of-findings.pdf>

<sup>12</sup> DSS, Register of Harm Prevention Charities – Guidelines, June 2017: <https://www.dss.gov.au/communities-and-vulnerable-people/programs-services/register-of-harm-prevention-charities/register-of-harm-prevention-charities-guidelines>

<sup>13</sup> Section 18(h) of the *Income Tax Assessment Act 1915*.

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subsequent legislation).<sup>14</sup> In the Parliamentary debates in 1927 there was an interesting discussion about the decision to include ‘public universities’ but not schools<sup>15</sup> as well as discussion about how the Commissioner of Taxation could be sure that entities really were ‘public charitable institutions if that term was not defined.<sup>16</sup> The legislation also provided ‘that payments shall not be allowable as deductions under this paragraph unless verified to the satisfaction of the Commissioner’<sup>17</sup> although this requirement had disappeared by the rewrite of 1936.

In the rewrite of the tax legislation in the *Income Tax Assessment Act 1936* (ITAA 1936) the wording had changed to expand the range of eligible recipients in s 78 of that Act as follows:

- (i) a public hospital;
- (ii) a public benevolent institution;<sup>18</sup>
- (iii) a public fund established and maintained for the purpose of providing money for public hospitals or public benevolent institutions in Australia, or for the establishment of such hospitals or institutions, or for the relief of persons in Australia who are in necessitous circumstances;
- (iv) a public authority engaged in research into the causes, prevention or cure of disease in human beings, animals or plants, where the gift is for such research, or a public institution engaged solely in such research;
- (v) a public university or a public fund for the establishment of a public university;
- (vi) a residential educational institution affiliated under statutory provisions with a public university, or established by the Commonwealth; and
- (vii) a public fund established and maintained for providing money for the construction or maintenance of a public memorial relating to the [first world war].<sup>19</sup>

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<sup>14</sup> *Income Tax Assessment Act 1927*. See also A O’Connell and J Chia, ‘Charitable Treatment? — A Short History of the Taxation of Charities in Australia, Vol 5’ in John Tiley (ed), *Studies in the History of Tax Law* (Hart Publishing, 2011).

<sup>15</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 29 November 1927, 2159.

<sup>16</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 29 November 1927, 2168. A definition of ‘public charitable institution’ was then inserted into into 18(h) by the *Income Tax Assessment Act 1927*: the term was defined as meaning “a public hospital, a public benevolent institution and includes a public fund established and maintained for the purpose of providing money for such institutions or for the relief of persons in necessitous circumstances.”

<sup>17</sup> Section 18(h) of the *Income Tax Assessment Act 1915*.

<sup>18</sup> The term ‘public benevolent institution’ appears to have been used in the legislation in response to the Privy Council decision in *Chesterman v FCT* [1925] 37 CLR 317, that held that ‘charity’ in Australia had a legal meaning based on the decision in *Commissioners for Special Purposes of the Income Tax v Pemsell* [1891] AC 531, rather than its ordinary meaning.

<sup>19</sup> Section 78 of the *Income Tax Assessment Act 1936*.

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Over the next 57 years there were 34 amending Acts that increased the number of eligible entities or types of entities to 110. The amendments appear to be ad hoc – perhaps in response to the perceived limited nature of the categories eg in 1951, NFP hospitals were included, in 1954 the Australian Academy of Science and school building funds and in 1966 the Australian Conservation Foundation Incorporated. Other amendments appear to be in response to various natural disasters or the death of a prominent person eg in 1965 the Winston Churchill Memorial Trust was included and in 1978 the Sir Robert Menzies Memorial Trust.

In 1993 the *Taxation Laws Amendment (No 2) Act 1993* reorganised the listing into categories that are fairly similar to those that are now in the ITAA 1997. That exercise does not appear to have been a substantial revision of the entities that had been afforded DGR status but rather a ‘cleaning up’ or rationalisation of the content of section 78.

The rewrite of the Income Tax Assessment Act in 1997 introduced a Table in s 30-15(1) that sets out ‘gifts or contributions you can deduct’. There are now 8 items in that Table. Item 1 refers to ‘a fund, authority or institution covered by an item in any of the Tables in Subdiv 30-B and includes the type of gift (money or property); how much can be deducted and some special conditions, including the ‘in Australia’ condition and the requirement for some, but not all entities to be endorsed by the Commissioner of Taxation. There are separate items for ‘the Australiana Fund, a public libraries, public museums and public art galleries (although these are also general categories in Subdiv 30-B), Artbank and the various branches of the National Trust (although they are also included in the general categories in Subdiv 30-B). Subdiv 30-B contains 46 general categories (including the 4 Registers) grouped under 14 headings. The headings are discussed in Part 5.

Since 2012 some, but not all, of the entities are required to be a registered charity (ie charity registered by the ACNC) or be an Australian government agency.

## (II) LISTING

As noted above the practice of including entities by name started because of concern that those entities would not fall within existing categories. It might have been thought that the reorganisation of the entities in 1993 which included ‘general categories’ would reduce the need for specific listing but this has not been the case with numerous amending Acts in the intervening years that have added (or less often removed) specific entities. There are several problems with the inclusion of specific entities in the DGR framework:

- The process is time consuming for the entity, lacks transparency and involves valuable legislative resources;
- Specifically listed entities are not required to be registered with the ACNC or to be endorsed by the Commissioner of Taxation. Specifically listed entities are therefore not required to provide any information about their activities; and

- There is no provision for review of entitlement so that effectively entitlement continues indefinitely.

### (III) FOUR REGISTERS

The registers have developed at different times and for different reasons, including it would seem a view that certain entities should be subject to some sort of approval process and perhaps regulatory oversight.

The first 'register' to be included in the ITAA was the **Overseas Aid Gift Deduction Scheme** established by *Income Tax Law Amendment Act 1981* and operated by the Department of Foreign Affairs and Trade (DFAT). The reason for establishing the scheme and requiring approval by DFAT was presumably because of the 'in Australia' requirements. DFAT also notes that "there is a high degree of risk in undertaking overseas development activities, [and so the scheme] seeks to ensure that organisations applying for [approval] have good governance structures in place and a high standard of international development practice, based on their track record".<sup>20</sup> It has also been noted that there are unique challenges involved in providing assistance to developing countries and the need to have safeguards in place and manage risks associated with child protection and terrorism.<sup>21</sup> DFAT declares which countries are 'developing countries' for these purposes. DGR status is provided under s 30-80, Item 9.1.1 and s 30-85 of the ITAA 1997. Since 2012 the entity must be a registered charity ie registered under the *ACNC Act 2012*. The OAGDS Guidelines issued by DFAT (updated in February 2016) set out the other criteria for approval ie the entity must have a board of management that does not receive remuneration; must demonstrate its ability to manage and deliver its aid activities; demonstrate how it works with developing country partner organisations and that it has appropriate safeguards in place and manages risks associated with child protection and terrorism. The entity must maintain a public fund for donations.<sup>22</sup> The current position is that DFAT provides approval for an organisation that meets the eligibility criteria and maintains the public fund, the entity is then gazetted by the Treasurer and becomes eligible to be endorsed as a DGR by the Commissioner of Taxation. DFAT does not appear to maintain a separate register or to require any regular reporting<sup>23</sup> or compliance additional to that of the ACNC.

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<sup>20</sup> OAGDS, Frequently Asked Questions: <http://dfat.gov.au/about-us/publications/Documents/oagds-frequently-asked-questions.pdf>

<sup>21</sup> DFAT OAGDS Guidelines February 2016: <http://dfat.gov.au/about-us/publications/Documents/oagds-guidelines.pdf>

<sup>22</sup> In accordance with s 30-130 ITAA 1997. The ATO provides guidance on the Overseas Aid Gift Deduction Scheme in TR 95/2 although this still refers to s 78 of the ITAA 1936.

<sup>23</sup> DFAT may request an organisation to provide information that demonstrates the organisation is operating in accordance with the OAGDS guidelines: see OADGS Frequently Asked Questions, n 10. Failure to do so may result in endorsement being revoked.

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The second register to be established was the **Register of Cultural Organisations** was established by the *Taxation Laws Amendment (No 3) Act 1991* and is administered by the Department of Communication and the Arts. In 1991 it was noted that there were 7 cultural organisations listed in s 78 but over the course of 1991 a further 172 organisations were identified as cultural organisations.<sup>24</sup> The reason for establishing the Register was so that individual cultural organisations would not need to seek listing in the ITAA 1936<sup>25</sup> and to encourage donors to give to approved cultural organisations.<sup>26</sup> The legislation provided that eligibility would be available to entities that had the 'principal purpose of promotion of literature, music, a performing art, a visual art, a craft, design, film, television, radio, community arts, arts of indigenous persons or movable cultural heritage'.<sup>27</sup> DGR status is provided by s 30-100, Item 12.1.1 and Subdiv 30-F. The requirements are discussed in Guidelines published by the Department in 2008.<sup>28</sup> The entity must be a body corporate or a trust or a statutory body ie an unincorporated body established for a public purpose by government<sup>29</sup> and must maintain a public fund in accordance with s 30-130 ITAA 1997.<sup>30</sup> In a variation of the NFP requirement, the entity must not pay any of its profits or surplus or give any property to its members, beneficiaries, controllers or owners.<sup>31</sup> There is also a requirement to provide statements of gifts made to the public fund every six months<sup>32</sup> and to undergo a review every three years.<sup>33</sup> An approved organisation is also eligible to participate in the Cultural Gifts program which also provides CGT relief.<sup>34</sup> The approved entity must also be endorsed by the ATO.<sup>35</sup> Approval may be withdrawn and the entity removed from the Register.<sup>36</sup> Although inclusion on the Register entitles the entity to DGR status, this process is separate from the registration requirements under the *ACNC Act* which would be required for other tax concessions. There are currently more than 1000 entities on the register.

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<sup>24</sup> Explanatory Memorandum to the Taxation Laws Amendment (No 3) Bill 1991.

<sup>25</sup> There are, however, currently four listed entities.

<sup>26</sup> Explanatory Memorandum to the Taxation Laws Amendment (No 3) Bill 1991.

<sup>27</sup> See now s 30-300(2) ITAA 1997.

<sup>28</sup> Register of Cultural Organisations Guidelines 2008:

<https://www.arts.gov.au/sites/g/files/net1761/f/RegisterOfCulturalOrganisationsGuide.pdf>

<sup>29</sup> Section 30-300(1) ITAA 1997.

<sup>30</sup> Section 30-300(3) ITAA 1997.

<sup>31</sup> Section 30-300(5) ITAA 1997.

<sup>32</sup> Section 30-300(7) ITAA 1997.

<sup>33</sup> See ROCO Guidelines, n 17.

<sup>34</sup> Section 118-60(2) ITAA 1997. The Department has a Guide to the Cultural Gifts Program published in September 2016: <https://www.arts.gov.au/documents/cultural-gifts-program-guide-tax-incentives-cultural-gifts-australias-public-collections>

<sup>35</sup> See ROCO Guidelines, n 17.

<sup>36</sup> Section 30-310 ITAA 1997 and see ROCO Guidelines, n 17.

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The third register is the **Register of Environmental Organisations** was established in 1992 by *Taxation Law Amendment (No 5) Act 1992* and is maintained by the Department of the Environment. The first environmental entity to be given DGR status was the Australian Conservation Foundation Incorporated which was listed by name as a DGR in s 78 in 1966. Between 1966 and 1990 a further 12 environmental organisations were listed by name in the ITAA 1936. With so few approved entities some acted as ‘conduits’ for other environmental organisations that did not have the resources to become listed. The purpose of establishing the Register was said to be “to streamline the process for environmental organisations to obtain DGR status, to increase transparency of access to tax-deductible donations and to enhance fundraising by such entities”.<sup>37</sup> DGR status is provided by s 30-55 and Subdiv 30-E of the ITAA 1997. Subdiv 30-E sets out the types of entities that are eligible for registration (a body corporate, a cooperative, a trust or a statutory body)<sup>38</sup> and provides that the principal purpose must be “the protection and enhancement of the natural environment or of a significant aspect of the natural environment, or the provision of information or education, or the carrying on of research, about the natural environment or a significant aspect of the natural environment”.<sup>39</sup> The legislation also provides that registered entities must not act as ‘mere conduits’ for monies to be transferred to other organisations or persons<sup>40</sup> and that the entity must provide statistical information about gifts to the public fund annually.<sup>41</sup> Registered entities must also comply with any Ministerial Rules.<sup>42</sup> There are currently two such Rules set out in Guidelines (last updated in 2003):<sup>43</sup> Ministerial Rule 1 that provides that the annual statement is to provide information on the expenditure of public fund monies and the management of public fund assets; and Ministerial Rule 2 that provides that the organisation must inform the Department about any changes to its name, membership of the management committee or any departure from the Model Rules of the public fund. The Guidelines set out the grounds for removal under s 30-285 as follows:

- no longer meeting the requirements of the ITAA; or
- not collecting tax-deductible donations from the public; or
- not using donations to the public fund for the principal purposes of the environmental organisation; or

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<sup>37</sup> Explanatory Memorandum to the Taxation Laws Amendment (No 5) Bill 1992.

<sup>38</sup> Section 30-260 ITAA 1997.

<sup>39</sup> Section 30-265(1) ITAA 1997.

<sup>40</sup> Section 30-270(2) ITAA 1997.

<sup>41</sup> Section 30-270(4) ITAA 1997.

<sup>42</sup> Section 30-265(4) ITAA 1997.

<sup>43</sup> Department of Environment, Register of Environmental Organisations Guidelines 2003:

[http://www.environment.gov.au/system/files/pages/53ca6702-48ad-414a-bf24-60e253d5ad0d/files/reo-guide-2003\\_0.pdf](http://www.environment.gov.au/system/files/pages/53ca6702-48ad-414a-bf24-60e253d5ad0d/files/reo-guide-2003_0.pdf)

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- not adhering to the Model Rules for public funds as set out in Section 7 of the Guidelines.<sup>44</sup>

When an environmental entity has been registered, the Department notifies the Commissioner of Tax in writing so that the entity can be endorsed. Entities listed by name in Div 30 of the ITAA 1936 are not required to comply with the same requirements for registration with the Department or endorsement and are not required to comply with the requirements applicable to registered environmental entities. Currently, 596 environmental organisations are listed on the Register.

The Report into the Register of Environmental Organisations (REO Report) noted that the process for registration is lengthy and complex, lacks transparency and involves duplication and overlap.<sup>45</sup> Although inclusion on the Register entitles the entity to DGR status, this process is separate from the registration requirements under the ACNC Act which is required for other tax concessions. The REO Report noted that approximately 75 per cent of organisations listed on the Register are also registered charities and that in 2013–14, registered charities received 99 per cent of the value of donations to organisations listed on the Register.<sup>46</sup> The REO Report concluded that registration as a charity through the ACNC should be a prerequisite for obtaining DGR status as an environmental organisation. Furthermore, the Committee considered that the process of DGR endorsement should be transferred completely to the ATO.<sup>47</sup>

The fourth register is the **Register of Harm Prevention Charities** established in 2003 by *Taxation Laws Amendment (No 6) Act 2003* and administered by the Department of Social Services. The Register was announced by the Treasurer as part of the government response to the Charities Definition Inquiry (CDI).<sup>48</sup> This does not seem to have been in response to any particular recommendation of the CDI although there were comments that the notion of a Public Benevolent Institution required direct action and so may exclude organisations that engage in educative or preventative activities.<sup>49</sup> DGR status is provided for the public fund by s 30-45, Item 4.1.1 which must be a registered charity or operated by a registered charity, and Subdiv 30-EA which provides for eligibility for the institution operating the public fund. In addition to being a registered charity, the entity must be endorsed as income tax exempt by the Commissioner of Taxation before it can apply to become a registered

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<sup>44</sup> Ibid, Section 5.

<sup>45</sup> House of Representatives Standing Committee on the Environment, Inquiry into the Register of Environmental Organisations under the ITAA 1997, Report May 2016, para 2.33:  
[http://www.aph.gov.au/Parliamentary\\_Business/Committees/House/Environment/REO/Report](http://www.aph.gov.au/Parliamentary_Business/Committees/House/Environment/REO/Report)

<sup>46</sup> Ibid, para 3.79.

<sup>47</sup> Ibid, Recommendations 1, 4, 7, 8 and 9.

<sup>48</sup> Treasurer's Press Release No 49 of 2003 (29 August 2003).

<sup>49</sup> Charities Definition Inquiry, Report, June 2001 eg at p 167.

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harm prevention charity. To be a harm prevention charity, the principal activity of the institution must be the promotion of the prevention or the control of human behaviour that is harmful or abusive to human beings.<sup>50</sup> Behaviour that is harmful or abusive is defined in s 995-1 of the ITAA 1997 to mean one or more of the following:

- Emotional abuse
- Sexual abuse
- Physical abuse
- Suicide
- Self-harm
- Substance abuse
- Harmful gambling.

The requirements set out in Subdiv 30-EA and the departmental Guidelines (revised in June 2017) are similar to those for entities on the REO ie the entity must maintain a public fund,<sup>51</sup> provide statistical information about donations and expenditure annually to the Department<sup>52</sup> and not act as a conduit for other entities.<sup>53</sup> When approval is granted the Department forwards the application to the Commissioner for Taxation to determine DGR status for the public fund under s 30-45, Item 4.1.4. There is also provision for removal of a fund from the Register.<sup>54</sup> There are currently 78 registered Harm Prevention Charities.

All four registers appear to have been introduced either because there were doubts about whether they fitted into existing categories and/or before there was an independent regulator capable of overseeing the particular types of entities. It seems likely that all of the entities on the Registers would be 'charities' as defined by the *Charities Act* or government entities. Apart from the common requirement to maintain a gift fund (discussed below) there are varying additional requirements. It would be a matter for government to decide whether those matters merit ongoing oversight by the particular government department. In this regard it is interesting to note that the REO report recommended that regulation and oversight be removed from the Department for the Environment and shared between the ACNC and ATO. We also suspect that the entities on the Register of Harm Prevention Charities could be regulated by the ACNC. There may, however, be good reasons for DFAT to

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<sup>50</sup> Section 30-289 ITAA 1997.

<sup>51</sup> Section 30-289(2) ITAA 1997.

<sup>52</sup> Section 30-289A(3) ITAA 1997 and Guidelines: <https://www.dss.gov.au/communities-and-vulnerable-people/programs-services/register-of-harm-prevention-charities/register-of-harm-prevention-charities-guidelines>

<sup>53</sup> Section 30-289A(1) ITAA 1997.

<sup>54</sup> Section 30-289C ITAA 1997 and Guidelines Section 10. Note that the reasons for removal listed in the Guidelines are similar to those for an Environmental Organisation but also include 'engaging in illegal activities'.

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continue to have a role in monitoring entities that deliver aid overseas and perhaps for the Department for the Arts to have a role in approving, in particular, what constitutes a 'cultural gift'.

#### (IV) THE ACNC; THE CHARITIES ACT AND PAFs

The last time the structure of the DGR regime was overhauled was in 1993 when the general categories were established. Despite the existence of the general categories, specific listing has continued and as noted in the Discussion Paper there are currently 190 entities listed. These entities are not required to be endorsed and in general their status continues indefinitely.

The DGR framework has also not sufficiently adapted to other changes in related areas. The first general matter to note is that the reason for seeking DGR status may have changed since the introduction of Private Ancillary Funds (PAFs).<sup>55</sup> In the past the reason for seeking DGR status was to be able to receive gifts that could then be claimed as a deduction by the donor. Since the introduction of PAFs (and the growth of Public Ancillary Funds (PuAFs)<sup>56</sup>) entities seeking grants from PAFs or PuAFs must themselves be DGRs so many entities applying for DGR status may not be seeking funds from the public and this may have consequences for how entities that do not seek to raise funds from the public should be regulated.

The second significant development has been the establishment of the ACNC in December 2012. The REO Report identified some of the inconsistencies in the DGR framework in relation to the ACNC. Many entities within the general categories, but not all, are required to be (or in the case of a fund, to be operated by) a registered charity or an Australian government agency or, in some cases, not be an ACNC type entity.<sup>57</sup> Entities within Subdiv

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<sup>55</sup> Private Ancillary Funds (PAFs) started life as part of the Howard Government's response to a March 1999 report by the Business and Community Partnerships Working Group on Taxation Reform to improve philanthropy in Australia. This led to the introduction of the Prescribed Private Fund (PPF) being available as a philanthropic structure and the first PPF funds were established in June 2001. In November 2008, the Rudd Government released a discussion paper on "Improving the Integrity of PPFs". After extensive consultation, new legislation and guidelines were released converting PPFs to PAFs from 1 October 2009. There are currently more than 1300 PAFs in Australia. For information about PAFs generally, see Philanthropy Australia: <http://www.philanthropy.org.au/>

<sup>56</sup> Public Ancillary Funds (PuAFs) have existed for some time but the regulatory requirements for these funds were brought more into line with those requirements for PAFs in 2011. PAFs and PuAFs are subject to Guidelines that include mandatory minimum distribution requirements and the requirement to lodge an annual information return with the ATO: see <https://www.legislation.gov.au/Details/F2016C00435> for PAFs and <https://www.legislation.gov.au/Details/F2011L02758> for PuAFs.

<sup>57</sup> Div 30 refers to the entity being a 'registered charity' or 'not an ACNC type of entity'. An ACNC type of entity is defined in s 995-1 ITAA 1997 as an entity that is eligible to be registered under s 25-5 of the ACNC Act 2012. So the reference to 'not an ACNC type entity' is to an entity that is not eligible to be registered as a charity.

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30-B, other than entities that are specifically listed, must then be endorsed by the Commissioner of Taxation.<sup>58</sup> This includes government entities.<sup>59</sup> Two of the four registers require entities to be registered with the ACNC – the OAGDS and the Register of Harm Prevention Charities but the other two do not. Some of these entities may choose to become registered in order to access other tax concessions. Specifically listed entities are not required to be registered or to be endorsed by the ATO.

The third significant development is the introduction of the statutory definition of ‘charity’ and ‘charitable purpose’ for all Commonwealth purposes in the *Charities Act*. Although the DGR provisions are not based on whether an entity is a charity, there is now greater similarity between the notion of what constitutes a charity and the categories in the DGR provisions. The statutory definition of charity and how it relates to DGR status is discussed below in Part 5.

#### 4. THE POSITION IN OTHER JURISDICTIONS

Most jurisdictions provide some form of tax relief for donations to various entities. However, there are significant differences between jurisdictions as to (i) the type of tax relief (ii) the conditions or restrictions imposed and (iii) the types of entities eligible to receive these gifts and the process for approval of such entities. For purposes of comparison we have considered the rules relating to gift tax concessions in the United Kingdom, Canada, New Zealand and the United States.

##### (I) TYPE OF RELIEF

Australia provides a deduction for both individual taxpayers and corporate taxpayers.

- Some jurisdictions provide a tax credit rather than a deduction: Canada<sup>60</sup> and New Zealand;<sup>61</sup>
- Some jurisdictions have different incentives for individuals and corporations: Canada and New Zealand provide a tax credit for individuals and a deduction for corporations;<sup>62</sup>
- The United Kingdom has Gift Aid for individuals<sup>63</sup> and allows a deduction for corporations.<sup>64</sup>

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<sup>58</sup> Endorsement by the Commissioner of Taxation is provided for in Subdiv 30-BA of the ITAA 1997 and Div 426, Sched 1 of the *Taxation Administration Act 1953*.

<sup>59</sup> Section 30-180 ITAA 1997.

<sup>60</sup> Section 118.1 *Income Tax Act 1985* (Canada).

<sup>61</sup> Section LD 1 *Income Tax Act 2007* (New Zealand).

<sup>62</sup> Section 110.1 *Income Tax Act 1985* (Canada) and s DB 41 *Income Tax Act 2007* (New Zealand).

<sup>63</sup> Section 414 *Income Tax Act 2007* (UK). Gift Aid allows charities in the United Kingdom to claim back the basic rate tax paid on donations by the donor. This means the charity can claim from the government 25p for

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## (II) CONDITIONS OR RESTRICTIONS

The gift in Australia may be cash or property.<sup>65</sup> There is a \$2 minimum for gifts of cash (unchanged since 1927) but no maximum ie a taxpayer is entitled to deduct 100% of the gift up to the taxpayers taxable income for the year.<sup>66</sup> There are also spreading rules in the case of gifts of property. Property may be real or personal property including trading stock and there are valuation rules that must be used to determine the value of the property.<sup>67</sup> There is no definition of gift but case law indicates that the gift must be voluntary and that no significant benefit can be received by the donor.<sup>68</sup> There are some quite restrictive rules that deal with fundraising events such as gala dinners and charity auctions.<sup>69</sup> There are some conditions that are specific to certain DGRs and all gifts to entities within Subdiv 30-B must satisfy the 'in Australia' condition<sup>70</sup> (which is different to the requirement for income tax exemption in Div 50 ITAA 1997).

- In the United Kingdom, Gift Aid only applies to gifts of money,<sup>71</sup> but there are separate rules for gifts of real property and shares;<sup>72</sup> the other jurisdictions permit gifts of cash or property although there are some restrictions on gifts of trading stock (inventory) in Canada;<sup>73</sup>
- Most jurisdictions impose limits in relation to the amount of the relief;<sup>74</sup>
- Valuation rules tend to be less complex, relying on the notion of 'fair market value' but with appropriate anti-avoidance rules;<sup>75</sup>

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every £1 donated (provided the donor has paid sufficient tax in the United Kingdom). Higher rate taxpayers can claim the difference between the higher rate and basic rate on the donation.

<sup>64</sup> Section 189 *Corporations Tax Act 2010* (UK).

<sup>65</sup> Section 30-15, Item 1, column 2 ITAA 1997.

<sup>66</sup> Section 26-55(1)(ba) ITAA 1997.

<sup>67</sup> Section 30-15(1), Item 1, column 2 and Subdiv 30-C ITAA 1997.

<sup>68</sup> See Taxation Ruling TR 2005/3 *What is a gift?*

<sup>69</sup> Section 30-15(1), Items 7 and 8 ITAA 1997.

<sup>70</sup> Section 30-15(1), Item 1, column 4, ITAA 1997.

<sup>71</sup> Section 416(2)(a) *Income Tax Act 2007* (UK).

<sup>72</sup> Section 431 *Income Tax Act 2007* (UK).

<sup>73</sup> See Canada Revenue Agency Policy Commentary, *Gifts out of Inventory*: <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cpc/cpc-018-eng.html>

<sup>74</sup> In New Zealand, individuals can claim a tax relief equal to 33.3 per cent of the gift: s LD 1 *Income Tax Act 2007*. In Canada both individuals and corporations are subject to limits on tax relief of 75 per cent of their net income. There are also limits on the amount of tax credit an individual can claim depending on the amount of the gift and the level of net income: see Canada Revenue Agency Guide: <http://www.cra-arc.gc.ca/chrts-gvng/dnrs/svngs/clmng1-eng.html>. In the United States, contributions to charitable organisations may be deducted up to 50 percent of adjusted gross income. Contributions to certain entities ie private foundations, veterans organisations, fraternal societies, and cemetery organisations are limited to 30 percent of adjusted gross income: s 170 *Internal Revenue Code* (US).

- Several countries define what is meant by a gift;<sup>76</sup> and
- Most countries require proof of the gift ie a receipt.<sup>77</sup>

### (III) ELIGIBILITY

Australia, as noted, has a complex framework for eligibility: an introductory table with 8 items; general categories comprising 42 types of entities; 190 specifically listed entities and 4 separate registers that are administered by separate government departments. Some, but not all, eligible entities must be registered by the ACNC and some, but not all, must be endorsed by the ATO.

- No other jurisdiction has the complexity of the Australian regime and in particular no other jurisdiction lists particular entities within the legislation;
- The United Kingdom provides tax relief for gifts to charities and approved community amateur sports clubs (CASCs),<sup>78</sup> Canada provides tax relief for gifts to registered charities and some other qualified donees eg registered Canadian amateur athletic associations and certain approved public bodies;<sup>79</sup> New Zealand provides tax relief to 'charitable or other public benefit gifts'<sup>80</sup> and the United States provides relief for gifts to entities that are 'organised and operated exclusively for religious, charitable, scientific, literary or educational purposes, or to foster national or international amateur sports competition or for the prevention of cruelty to children or animals'.<sup>81</sup>

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<sup>75</sup> See Canada Revenue Agency Guide on Determining Fair Market Value: <http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rcpts/dtrmnfmv-eng.html> and US Internal Revenue Service Guidance: <https://www.irs.gov/pub/irs-pdf/p561.pdf>

<sup>76</sup> In the United Kingdom there is a definition of a 'qualifying donation' which includes requirements that the gift be unconditional and only 'minor benefits' are received in return: ss 416 to 418 *Income Tax Act 2007* (UK). In New Zealand, the gift must be 'unconditional': see <http://www.ird.govt.nz/non-profit/np-donations/donee/np-donee-claiming-tax-credits.html>

<sup>77</sup> Section 118.1(2) *Income Tax Act 1985* (Canada) and see also the rules for split receipting if a benefit is received by the donor: <http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtng/rcpts/splt-eng.html>; s LD 1(4) *Income Tax Act 2007* (New Zealand) and Section 170(a)(1) *Internal Revenue Code* (US) re verification.

<sup>78</sup> See United Kingdom Her Majesty's Revenue and Customs: <https://www.gov.uk/donating-to-charity/overview>.

<sup>79</sup> See Canadian Revenue Agency: <http://www.cra-arc.gc.ca/chrts-gvng/lstngs/lstchrts-qds-eng.html>

<sup>80</sup> This term is defined in s LD 3 as a gift to 'a society, institution, association, organisation, or trust that is not carried on for the private pecuniary profit of an individual, and whose funds are applied wholly or mainly to charitable, benevolent, philanthropic, or cultural purposes within New Zealand'.

<sup>81</sup> Section 170(c)(2)(B) *Internal Revenue Code* (US).

- The United Kingdom and New Zealand have a separate entity that determines eligibility for ‘charities’.<sup>82</sup> The Canadian Revenue has a separate Directorate that determines eligibility and confers registered status on charities. The United States Internal Revenue Service provides approval to exempt charitable organisations that are then eligible to receive deductible gifts.<sup>83</sup>
- Civil law countries do not use the term charitable but have a list of ‘worthy’ purposes that essentially reflect the common law notion of charity.

## 5. THE CURRENT POSITION

As noted above Div 30 of the ITAA 1997 provides for gift deductibility for 46 general categories (including the four Registers) and a large number of specific recipients. We have also noted the different requirements for different types of entities seeking DGR status, for example, some DGRs must be registered charities and so are subject to the governance and reporting requirements under the *ACNC Act*. The legislation dealing with eligibility for gift deductibility contains 320 sections and extends for 100 pages in the legislation and this does not include the provisions dealing with endorsement that are to be found in the *Tax Administration Act 1953*. According to ATO statistics<sup>84</sup> in the 2014-2015 financial year 4.57 million individuals claimed deductions for donations to DGRs totalling in excess of \$3 billion, an average claim of approximately \$675. This is an increase from the previous financial year when 4.5 million individuals made an average of \$576 with a total of \$2.6 billion.<sup>85</sup>

In this Part we consider two other matters that should be taken into account in any review of the gift deductibility provisions: the cost of providing the DGR concession and the increased similarity between the notion of what constitutes a charity and the DGR categories.

### (i) COST

The cost of providing gift deductibility has risen significantly in the last 20 years according to Treasury’s Expenditure Statements. Prior to 1996/97 Treasury did not provide separate estimates for revenue foregone in relation to gifts to approved donees under s 78 ITAA 1936. The following table indicates the estimated ‘cost’ of the gift deduction and from 2006/07 the additional ‘cost’ of the deduction for Ancillary Funds.

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<sup>82</sup> In the United Kingdom, this will be either the Charity Commission for England and Wales, the Office of the Scottish Charity Regulator or the Charity Commission for Northern Ireland. In New Zealand this is Charities Services, which is part of the Department of Internal Affairs, and administers the *Charities Act 2005* (NZ).

<sup>83</sup> See IRS Guidance: <https://www.irs.gov/charities-non-profits/application-for-recognition-of-exemption>.

<sup>84</sup> ATO Statistics 2014-2015 published in April 2017: <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Taxation-statistics/Taxation-statistics-2014-15/?anchor=Individuals#Table4>

<sup>85</sup> Ibid.

	<b>Cost of deduction for gifts to approved donees under Item 1, s 30-15 ITAA 1997</b>	<b>Cost of deduction for gifts to ancillary funds under Item 2, s 30-15 ITAA 1997</b>
1996/97	\$195m	Na
2000/01	\$276m	Na
2006/07	\$710m	\$75m
2010/11	\$1.07bn	\$380m
2016/17	\$1.3bn	\$705m

## (ii) DGR STATUS AND THE DEFINITION OF CHARITY

Since the enactment of the statutory definition of charity, the similarity between that definition and the DGR categories becomes clearer. It is also possible to identify which 'charities' are not included as DGRs. Not all income tax exempt entities (in Div 50 ITAA 1997) will be charities but it seems likely that almost all DGRs will be charities, except those that are government entities. The current DGR categories in Subdiv 30-B are as follows:

1. Health
2. Education
3. Research
4. Welfare and Rights
5. Defence
6. Environment
7. Industry, Trade and Design\*
8. Family
9. International Affairs
10. Sport and Recreation\*
11. Philanthropic Trusts\*
12. Cultural Organisations
13. Fire and emergency (12A)
14. Other recipients (13)\*

(\* denotes specific entities only)

According to ATO Statistics<sup>86</sup> a very large proportion of eligible entities are Public Benevolent Institutions (PBIs) (35 percent). This is likely to reflect the fact that PBIs enjoy

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<sup>86</sup> ATO Statistics 2014-2015, published April 2017: <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Taxation-statistics/Taxation-statistics-2014-15/>

other significant tax concessions, including an exemption from Fringe Benefits Tax.<sup>87</sup> The top 10 types of DGRs by type as at 1 November 2016 are as follows:

<b>Deductible Gift Recipient by type</b>	<b>No</b>
Public Benevolent Institutions	9,907
School or college building fund	4,850
Public library	1,656
Ancillary Funds	1,634
Public fund on the register of cultural organisations	1,601
Health promotion charity	1,542
Private Ancillary Funds	1,449
Public fund for persons in necessitous circumstances	639
Public fund on the register of environmental organisations	619
Public museum	612

Under the *Charities Act*, a charity is defined as a not-for-profit entity all of the purposes of which are charitable purposes that are for the public benefit or incidental or ancillary to that purpose, none of the purposes are disqualifying purposes and the entity is not an individual, a political party or a government entity.<sup>88</sup>

Section 12(1) of that Act defines ‘charitable purpose’ to mean any of the following:

- (a) the purpose of advancing health;
- (b) the purpose of advancing education;
- (c) the purpose of advancing social or public welfare;
- (d) the purpose of advancing religion;
- (e) the purpose of advancing culture;
- (f) the purpose of promoting reconciliation, mutual respect and tolerance between groups of individuals that are in Australia;
- (g) the purpose of promoting or protecting human rights;
- (h) the purpose of advancing the security or safety of Australia or the Australian public;
- (i) the purpose of preventing or relieving the suffering of animals;
- (j) the purpose of advancing the natural environment;
- (k) any other purpose beneficial to the general public that may reasonably be regarded as analogous to, or within the spirit of, any of the purposes mentioned in paragraphs (a) to (j);

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<sup>87</sup> Section 57A *Fringe Benefits Tax Assessment Act 1986*.

<sup>88</sup> Section 5 *Charities Act 2013*.

- (l) the purpose of promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a State, a Territory or another country, if:
- (i) in the case of promoting a change – the change is in furtherance or in aid of one or more of the purposes mentioned in paragraphs (a) to (k); or
  - (ii) in the case of opposing a change – the change is in opposition to, or in hindrance of, one or more of the purposes mentioned in those paragraphs.<sup>89</sup>

Note also that ‘advancing’ is defined as including protecting, maintaining, supporting, researching and improving.<sup>90</sup>

DGR category (excluding those with only listed recipients)	Charitable purpose as defined in the <i>Charities Act 2013</i>
1. Health	(a) advancement of <b>health</b> . Nb advancement includes research: s 3 and the purpose of advancing health includes the purpose of preventing and relieving sickness, disease or human suffering: s 14.
2. Education	(b) advancement of <b>education</b>
3. Research	Nb advancement includes <b>research</b> : s 3.
4. Welfare and rights	(c) advancement of <b>social or public welfare</b> : Nb the purpose of advancing social or public welfare includes the purpose of relieving the poverty, distress or disadvantage of individuals or families; the purpose of caring for and supporting: (a) the aged; or (b) individuals with disabilities; the purpose of caring for, supporting and protecting children and young individuals (and, in particular, providing child care services) and the purpose of assisting the rebuilding, repairing or securing of assets after a disaster: s 15  (f) promoting <b>reconciliation, mutual respect and tolerance</b> between groups of individuals that are in Australia;  (g) promoting or protecting <b>human rights</b> ;  (i) preventing or relieving the <b>suffering of</b>

<sup>89</sup> Subsection 12(2) provides paragraph (l) of the definition of *charitable purpose* in subsection (1) is the only paragraph of that definition that can apply to the purpose of promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a State, a Territory or another country. Subsection 12(3) provides that for the purposes of the section, it does not matter whether a purpose is directed to something in Australia or overseas.

<sup>90</sup> Section 3 *Charities Act 2013*.

	<b>animals.</b>
5. Defence	(h) advancement of <b>safety and security</b> : the purpose of advancing the security or safety of Australia or the Australian public includes the purpose of promoting the efficiency of the Australian Defence Force: s 17
6. Environment	(j) protection of the <b>natural environment</b>
8. Family	Nb (c) advancement of <b>social or public welfare</b> includes the purpose of relieving the poverty, distress or disadvantage of individuals or families
9. International Affairs	Nb (c) advancement of <b>social or public welfare</b> : the purpose of advancing social or public welfare includes the purpose of relieving the poverty, distress or disadvantage of individuals or families; the purpose of caring for and supporting: (a) the aged; or (b) individuals with disabilities; the purpose of caring for, supporting and protecting children and young individuals (and, in particular, providing child care services) and the purpose of assisting the rebuilding, repairing or securing of assets after a disaster: s 15. Nb for the purposes of the <i>Charities Act</i> it does not matter that a purpose is directed to something in Australia or overseas: s 12(3).
12. Cultural Organisations	(c) Promotion of <b>culture</b> : Nb the purpose of advancing culture includes the purpose of promoting or fostering culture and the purpose of caring for, preserving and protecting Australian heritage: s 16
12A. Fire and emergency	(h) advancement of <b>safety and security</b> : the purpose of advancing the security or safety of Australia or the Australian public includes the purpose of promoting the efficiency of the Australian Defence Force: s 17

The main differences between DGR status and the statutory definition of charity are as follows:

- Religion is not included as a separate DGR category;
- The Education DGR category is limited;
- Some DGR entities are government entities;
- Entities must satisfy the 'in Australia' condition for DGR status.

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## Religion

According to the Australian Charities Report 2015,<sup>91</sup> 31.2 percent of charities in Australia list advancing religion as at least one of their purposes. The Report also notes that nearly 60 percent (58.9 percent) of entities whose main activity was religious receive more than 50 percent of their income from donations.<sup>92</sup> Religion per se is not included within the DGR categories, however according to the Charities Report, 10.6 percent of entities whose main activity is religious have DGR status.<sup>93</sup> Presumably this is because they operate a Public Benefit Institution or a hospital or educational entity that does qualify for DGR status. Although it is not possible to know how much Australians donate to religious entities, it seems likely that the amounts are quite high and that this is the case despite the lack of separate DGR status. We note that some overseas jurisdictions do provide DGR status to religious entities. We make no recommendation in this regard apart from noting that any such changes are a matter for parliament and should only occur after proper consultation and consideration.

## Education

The Education category lists 14 types of educational entities. This includes public universities,<sup>94</sup> public funds for the establishment of a public university,<sup>95</sup> associated residential institutions,<sup>96</sup> public funds for the purpose of providing religious education<sup>97</sup> or ethics education<sup>98</sup> and school building funds.<sup>99</sup> As noted previously, when public universities were first included as DGRs there was Parliamentary debate about why primary and secondary schools were not also included.<sup>100</sup> The item dealing with school building funds was added in 1954 and the interpretation of this item has caused some confusion and perhaps misapplication.<sup>101</sup>

We recommend that the Education category be expanded to include all approved educational institutions – primary, secondary and tertiary. Any concern that fees may be disguised as gifts can be met by ensuring that the definition of gift is robust enough to

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<sup>91</sup> Cortis, N, Young, A, Powell, A, Reeve, R, Simnett, R, Ho, K, and Ramia, I. Australian Charities Report 2015, (2016) Centre for Social Impact and Social Policy Research Centre, UNSW Australia, p 34:

<http://australiancharities.acnc.gov.au/download/>

<sup>92</sup> Ibid, p 58.

<sup>93</sup> Ibid, p 51.

<sup>94</sup> Section 30-25(1) Item 2.1.1.

<sup>95</sup> Section 30-25(1) Item 2.1.2.

<sup>96</sup> Section 30-25(1) Items 2.1.3 to 2.1.5.

<sup>97</sup> Section 30-25(1) Item 2.1.9.

<sup>98</sup> Section 30-25(1) Item 2.1.9A.

<sup>99</sup> Section 30-25(1) Item 2.1.10.

<sup>100</sup> See n 15.

<sup>101</sup> See TR 2013/2 *Income tax: school or college building funds*.

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exclude payments where the donor receives a benefit, other than a minor benefit. It seems unduly restrictive to permit gifts to school building funds but not, to say, a scholarship fund or some other legitimate educational purpose.

### Government

The *Charities Act* confirms the common law position that government entities cannot be charities. There are, however, a number of DGR categories that could be either a charity or a government entity and some that can only be government entities. We agree with the TCWG Report that there should be a separate DGR category or categories for charity-like government entities.

### In Australia

Div 30 requires the entity to be 'in Australia' which presumably means established and/or operating in Australia. The *Charities Act* does not require a charity to be carrying out its purposes in Australia.<sup>102</sup> We made a submission on the Exposure Draft released by Treasury in 2014 about changes to the 'in Australia' requirement and make no further comment on the suitability of this requirement. We simply note that this is a matter for the ATO rather than the ACNC to enforce as it relates to the availability of tax concessions.

Given the above, we consider that there is significant scope for aligning the DGR regime with the statutory definition of charity and requiring all DGRs to be registered charities and so subject to the regulatory oversight of the ACNC and endorsed by the ATO and subject to the same requirements as other endorsed entities unless there is a case made for different requirements. A separate category should provide DGR status for charity-like government entities.

## 6. ISSUES IN THE DISCUSSION PAPER

The Discussion Paper has suggested proposals aimed at **strengthening DGR governance arrangements, reducing administrative complexity** and the need for **integrity in relation to eligibility**.

We make the following comments before addressing the specific proposals raised in the Discussion Paper:

We believe that the current DGR regime lacks **consistency, transparency and accountability** for the following reasons:

- Some, but not all, entities that are DGRs are required to be registered charities;

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<sup>102</sup> Subsection 12(3) of the *Charities Act 2013*, provides that for the purposes of the section dealing with charitable purposes, it does not matter whether a purpose is directed to something in Australia or overseas.

- Some, but not all, entities that are DGRs are required to be endorsed by the Commissioner of Taxation;
- Registered charities that are on one of the four Registers may have double reporting requirements;
- Entities that are on one of the four Registers may be required to provide information statements to relevant departments about gifts and expenditures but this is not necessarily made public;
- The process for becoming a listed entity is opaque and entities listed by name in Subdiv 30-B of the ITAA 1997 are not subject to public scrutiny;
- The general categories have been added to over time with no clear policy basis eg in 2003 a new category, Health Promotion Charity was included as a DGR (s 30-20, Item 1.1.6). These charities are also entitled to significant Fringe Benefits Tax (FBT) concessions but they do not have to be on a register similar to Harm Prevention Charities. There does not appear to be any clear reason for different treatment of Harm Prevention Charities and Health Promotion Charities;
- There have also been other ad hoc amendments eg in 2013 a new category of education recipient was included in s 30-25, Item 2.1.9A relating to providing ethics education in government schools as an alternative to religious education;
- Only some DGRs are required to maintain a gift fund.<sup>103</sup> The gift fund provided a level of accountability for entities that are in receipt of money from the public. We agree with the TCWG that with the introduction of the ACNC as a regulator (including for most entities that are DGRs) there is no further need for the gift fund requirement; and
- DGR status appears to influence a number of other provisions eg the FBT exemption and the FBT rebate. Any changes to the DGR provisions should be considered as a whole and in line with NFP tax concessions.

We believe that the DGR regime is **overly complex** for the following reasons:

- The length and structure of the legislation is too complex requiring consideration of different Tables, various conditions and potentially approval by three separate bodies: the ACNC, the ATO and in some cases a government department;
- There should be clarification of what constitutes a 'Public Benevolent Institution' to take account of recent case law and clarification of what constitutes a 'Necessitous Circumstances Fund' as this term appears to be outdated;
- The Welfare and Rights category could be simplified to conform to the types of charity encompassed by the charitable purpose of 'advancement of social or public welfare' in s 12 of the *Charities Act*;

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<sup>103</sup> See TR 95/27 *Income Tax: the Gift Fund Requirement*.

- There should be statutory clarification of what constitutes a ‘gift’ perhaps based on the UK definition of a ‘qualifying donation’;
- If any of the four registers are to be retained there should be an attempt to have more uniformity between the requirements with differences only where necessary to reflect the reason for the involvement of the relevant department;
- We note that the ‘in Australia’ requirement in the DGR provisions is different to the ‘in Australia’ requirement in Div 50 which adds to the complexity;
- The reference to ‘non-ACNC type entity’ in Subdiv 30-B is unclear. Is this intended to refer to government entities that are included in Subdiv 30-B?
- The property valuation rules in Subdiv 30-C are complex and could be simplified.<sup>104</sup>

We believe that the **integrity** of the provisions could be improved by requiring entities to demonstrate periodically their continuing entitlement to eligibility. This could be achieved by the following:

- All DGRs should be either registered charities or approved government entities;
- Making all DGR entities that are eligible to become registered as charities by the ACNC do so. This will ensure greater transparency and accountability;
- Government entities (that are not eligible to be registered charities) should be required to be endorsed by the Commissioner of Taxation and, if thought necessary, approved by an appropriate Minister; and
- Review of the requirement for only some entities to be subject to the requirement about acting as ‘conduits’.

## ISSUES IN THE DISCUSSION PAPER RE STRENGTHENING GOVERNANCE ARRANGEMENTS

### Issue 1: Transparency in DGR dealings and adherence to governance standards

**Proposed Action:** All DGRs (other than government entities) to be registered as charities and regulated by the ACNC

We agree with the proposed action. This would ensure consistency of treatment and should remove duplication (subject to any perceived need to maintain the involvement of a government department such as DFAT). As only around 8 percent of DGRs (ie approximately 2,240) are not registered charities or government entities this should not be too onerous for the ACNC.

We agree that the proposed action is appropriate to require DGRs to be transparent in their dealings and to adhere to appropriate governance standards and, as noted, is consistent

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<sup>104</sup> See TCWG Report, Rec 8. It was noted that the requirement to be or to have a public fund is in part intended to ensure that moneys and property donated to the fund, which attract a tax concession, are used for the purpose for which the fund has been granted DGR status. With the introduction of the ACNC and an annual reporting requirement, it was felt that the public fund requirement involved unnecessary red tape.

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with a recommendation of the TCWG.<sup>105</sup> Although we expect that all entities other than government entities would be eligible to be registered as charities, we agree with the TCWG proposal that any entities that are not eligible as either a charity or government entity could make a special case for endorsement as a DGR.

In relation to privacy concerns we note that the ACNC has power to withhold information from the Register in appropriate cases and has done so with respect to Private Ancillary Funds.

**Recommendation 1:** All DGRs should be charities (as defined in the *Charities Act 2013*) or charitable-like government entities

## Issue 2: Ensuring that DGRs understand their obligations

### Proposed action: Require the ACNC to provide guidance on advocacy

We do not agree that entities, such as environmental organisations, or any other type of entities should be required to provide additional information about their advocacy activities. In this regard, we note that it has been recognized by the courts that advocacy by charities is not only permissible but is often an effective means of achieving a charitable purpose. Many other types of charities engage in advocacy and educational activities as the main, or one of, the ways of achieving their charitable purpose. One non-environmental entity example is BeyondBlue, which provides information about depression and suicide prevention as well as support to those at risk and lobbies government in relation to mental health.<sup>106</sup>

We also note that the permissible restrictions on advocacy have been outlined by the High Court in *Aid/Watch Inc v FCT*<sup>107</sup> and are now stipulated in the *Charities Act*,<sup>108</sup> in which case requiring entities to provide further detail about their advocacy activities could be in breach of the Act as there needs to be a sufficient connection with their entitlement to be a DGR and/or a charity.<sup>109</sup>

Finally, we note that where charities trespass into the field of forbidden advocacy (e.g. partisan political activities), it is very unlikely that this would be disclosed in a voluntary way,

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<sup>105</sup> TCWG Report, n 2, Rec 6.5.

<sup>106</sup> See <https://www.beyondblue.org.au>

<sup>107</sup> [2010] HCA 42.

<sup>108</sup> See s 12(1) of the *Charities Act* provides that a charity may have the purpose of promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a State, a Territory or another country, if the change is related to one or more of the purposes mentioned in paras (a) to (k) of the definition of 'charitable purpose': para (l). Subsection 12(2) provides that para (l) is the only paragraph of that definition that can apply to the purpose of promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a State, a Territory or another country.

<sup>109</sup>

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so that essentially any requirements are likely to be a poor form of regulation (as there will be additional red tape on compliant charities but unlikely to be any real data that would assist the ACNC in revoking registration) (and of course inimical to the purpose of the establishment of the ACNC).<sup>110</sup> The ACNC already has detailed guidance on what charities can and cannot do in relation to advocacy.<sup>111</sup>

There is no good reason why environmental or any other organisations should be required to provide separate information about advocacy. If it is believed that a registered charity is not pursuing its charitable purpose, the appropriate course would be to request the ACNC to investigate. If a registered charity engages in or encourages others to engage in criminal acts then the appropriate course is to refer the matters to the police.

**Recommendation 2:** That there is no need for any additional requirements for environmental organisations in relation to advocacy further than those contained in the *Charities Act* and subject to the guidance on advocacy provided by the ACNC.

### Issues in the Discussion Paper re Reducing Complexity

#### Issue 3: Complexity for approvals under the four DGR registers

##### Proposed action: Transfer administration of the four registers to the ATO

As noted in Part 3 we believe that the registers add a level of complexity – for registered charities there are two sets of requirements to comply with and for entities that are not currently registered charities, there are inconsistent requirements and in most cases, little transparency. However, in our view it would be better for entities on the register that are eligible to be charities to have administration transferred to the ACNC rather than the ATO. The ACNC is the regulatory body and has the expertise to deal with applications for approval as charities and to exercise supervision over such bodies. It should, however, still be up to the ATO to provide endorsement and this should only be concerned with whether any additional conditions or requirements are necessary for tax relief, such as the ‘in Australia’ requirement.

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<sup>110</sup> See Not-for-Profit Project Submission to House of Representatives Standing committee on the Environment Inquiry into the Register of Environmental Organisations (Submission 220, 18 May 2015): [http://www.aph.gov.au/Parliamentary\\_Business/Committees/House/Environment/REO/Submissions](http://www.aph.gov.au/Parliamentary_Business/Committees/House/Environment/REO/Submissions)

<sup>111</sup> See ACNC Fact Sheet, Charities and Advocacy: <http://www.acnc.gov.au/ACNC/Reg/Advocacy.aspx> and Guidance on Charities, Elections and Advocacy released April 2016: [http://www.acnc.gov.au/ACNC/Reg/Charities\\_elections\\_and\\_advocacy.aspx](http://www.acnc.gov.au/ACNC/Reg/Charities_elections_and_advocacy.aspx)

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**Recommendation 3:** The four registers in Div 30 of the *Income Tax Assessment Act 1997* (ITAA 1997) be reviewed by the relevant departments and the Assistant Treasurer to see whether it is appropriate to transfer the entities on the Registers to the Australian Charities and Not-for-profit Commission (ACNC) register and to be subject to be endorsed by the Commissioner of Taxation. We agree that this is appropriate for the Register of Environmental Organisations.

**Issue 4: Complexity and red tape created by the public fund requirements**

**Proposed action: the Public Fund requirement should be removed**

For the reasons noted above we agree with this course of action.

**Recommendation 4:** That once entities are registered by the ACNC there is no compelling reason for maintaining the gift fund requirement.

### **Issues in the Discussion Paper re Integrity**

**Issue 5: DGRs endorsed in perpetuity, without regular systemic review**

**Proposed action: Regular reviews by ACNC and/or ATO**

We agree that there should be regular reviews by both the ACNC and the ATO to ensure there is ongoing eligibility for registration as a charity and for endorsement as a DGR. We acknowledge that this will have resourcing implications but believe that a review every 3 or 5 years is necessary to maintain the integrity of the system and to ensure that only those entities still eligible to do so receive the valuable tax concessions.

**Recommendation 5:** That the ACNC and the Australian Tax Office (ATO) should conduct regular reviews to determine whether entities are still eligible for DGR endorsement.

**Issue 6: Specific listing of DGRs by Government**

**Proposed action: introduce sunset periods of no more than 5 years**

We have argued above that specific listing of entities should cease and that existing listed entities should be required to be registered as charities or, in the case of entities not eligible to be registered charities, endorsed by the Commissioner. This would make it unnecessary to have sunset periods. The regular reviews contemplated in Issue 5 should apply to all entities to ensure ongoing eligibility.

**Recommendation 6:** Specific listing should be removed with existing entities becoming registered charities (if appropriate) and endorsed by the Commissioner of Taxation, subject to review of continuing eligibility

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## 7. OTHER ISSUES

We believe that the operation of the DGR rules also raises a number of other issues. For example, we suggest Treasury consider the following matters:

- Modernise the anti-avoidance rules for gifts: The anti-avoidance rules for donations where the donor receives material private benefits (s 78A ITAA 1936) should be rewritten in a simplified form and included in ITAA 1997. In rewriting the anti-avoidance/private benefit rules regard should be had to whether the existing minor benefits rules for fundraising could be repealed and instead become subject to the anti-avoidance rules, with the aim of further simplifying existing arrangements;
- Remove the \$2 minimum gift requirement which has been in the legislation since 1927 and serves no useful purpose;
- Consider whether there should be a requirement for DGRs to provide receipts for gifts above a certain minimum as verification that a bona fide gift has been made;
- Simplify the valuation rules for gifts of property;
- Review the DGR category of Education to remove anomalies as well as anomalies between entities such as Health Promotion Charities and Harm Prevention Charities;
- Provide legislative guidance on the meaning of a 'gift'; the meaning of a PBI (eg a charity that advances social or public welfare) and consider using more modern terminology instead of 'necessitous circumstances fund'; and
- Consider the interaction of any changes made to the DGR provisions with the other tax concessions for the NFP sector, including the income tax exemption and the FBT concessions.

**Recommendation 7:** That Treasury give consideration to other issues related to the DGR provisions to avoid inconsistencies and anomalies developing in the tax concessions for the not-for-profit (NFP) sector.

## 8. CONCLUSION

We hope that our submission has addressed the issues raised for consideration in the Discussion Paper. Although we understand the desire to pursue 'bite-sized chunks' of the legislation for reform, we agree with the TCWG Report that the taxation of NFPs generally is "cumbersome, inequitable and anomalous". We urge Treasury to expand the scope of its review to consider some of the other pressing issues that the NFP sector has to deal with including income tax exemptions, reduced rate of tax for NFP companies, franking credit refunds, GST, mutuality as well as other issues relating to the DGR provisions.

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Please feel free to contact us if you wish to discuss any matters further, or would like access to any of the material to which we have referred. Our contact details are listed in Appendix A.

A list of our recommendations is in Appendix B.

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## APPENDIX A: NOT-FOR-PROFIT PROJECT, MELBOURNE LAW SCHOOL

The Not-for-Profit Project is based at the University of Melbourne Law School. The Project involves a comprehensive and comparative investigation of the definition, regulation, and taxation of the not-for-profit sector in Australia. The Australian Research Council has funded this Project which began in 2010. The Project aims have been to identify and analyse opportunities to strengthen the sector and make proposals that seek to maximise the sector's capacity to contribute to the important work of social inclusion and to the economic life of the nation.

The members of the Not-for-Profit Project are:

### **Professor Ann O'Connell**

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Ann is a Professor at the Melbourne Law School. She is also Special Counsel at Allens, a member of the Advisory Panel to the Board of Taxation and a member of the Public Rulings Panel and the GAAR Panel of the Australian Tax Office. Ann was a member of the Not-for-profit Tax Concession Working Group in 2012-2013.

### **Professor Matthew Harding**

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Matthew is a Professor at the Melbourne Law School. His published work deals with issues in moral philosophy, fiduciary law, equitable property, land title registration, and the law of charity. Matthew has also worked as a solicitor for Arthur Robinson & Hedderwicks (now Allens).

### **Dr Joyce Chia**

Joyce is Special Advisor to the Not-for-Profit Project. She holds a PhD from University College London. She has worked at the Australian Charities and Not-for-profit Commission, University of New South Wales, Australian Law Reform Commission, the Federal Court of Australia, and the Victorian Court of Appeal.

More information on the NFP Project can be found on the website at

<http://law.unimelb.edu.au/centres/cclsr/research/major-research-projects/defining-taxing-and-regulating-the-not-for-profit-sector-in-australia-law-and-policy-for-the-21st-century>.

### **Melbourne Law School**

The University of Melbourne, Victoria, 3010, Australia

W: [www.law.unimelb.edu.au](http://www.law.unimelb.edu.au)

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## APPENDIX B: RECOMMENDATIONS

### Recommendation 1:

All DGRs should be charities (as defined in the *Charities Act 2013*) or charitable-like government entities

### Recommendation 2:

That there is no need for any additional requirements for environmental organisations in relation to advocacy further than those contained in the *Charities Act* and subject to the guidance on advocacy provided by the ACNC.

### Recommendation 3:

The four registers in Div 30 of the *Income Tax Assessment Act 1997* (ITAA 1997) be reviewed by the relevant departments and the Assistant Treasurer to see whether it is appropriate to transfer the entities on the Registers to the Australian Charities and Not-for-profit Commission (ACNC) register and to be subject to be endorsed by the Commissioner of Taxation. We agree that this is appropriate for the Register of Environmental Organisations.

### Recommendation 4:

That once entities are registered by the ACNC there is no compelling reason for maintaining the gift fund requirement.

### Recommendation 5:

That the Australian Tax Office (ATO) should conduct regular reviews to determine whether entities are still eligible for DGR endorsement.

### Recommendation 6:

Specific listing should be removed with existing entities becoming registered charities (if appropriate) and being endorsed by the Commissioner of Taxation (if appropriate), subject to review of continuing eligibility.

### Recommendation 7:

That Treasury give consideration to other issues related to the matters raised in the Discussion Paper to avoid inconsistencies and anomalies developing in the tax concessions for the not-for-profit (NFP) sector.