



**Australian Government**

**Prime Minister's Community Business Partnership**

The Hon Kelly O'Dwyer MP  
Minister for Revenue and Financial Services  
Parliament House  
CANBERRA 2600

Dear Minister

Thank you for the letter of 23 May 2017 to Angela Perry inviting the Prime Minister's Community Business Partnership (the Partnership) to make a submission outlining its views, in response to the Government's discussion paper on Tax Deductible Gift Recipient (DGR) Reform Opportunities.

We congratulate the Government for taking steps to promote community discussion about DGR through the release of the paper.

The DGR framework set out in Division 30 of the Income Tax Assessment Act 1997 (Cth) is a crucial enabling element for philanthropic partnerships to achieve outcomes for Australian communities. The Partnership has previously advised Government that the current DGR framework is restricting donors and charities from addressing today's complex problems in a whole-of-community manner. The Partnership reiterated this at its last meeting with the Prime Minister and the Minister for Social Services on 18 April 2017.

Our consultations have found that issues related to DGR are seen as a major impediment across the sector. One of our roundtable participants summed up a broad view that *"The DGR framework is broken – it evolved in an ad-hoc manner, complex, riddled with red tape, inconsistent, and just a headache for charity lawyers and charities themselves"*.

For example, an organisation whose principal activity is to promote education is eligible for DGR status under the category of 'Education Charity'. However, when that organisation works 'upstream' to address family social engagement and welfare issues, it is unable to attract tax deductible donations for that purpose as it is not registered as a 'Welfare Charity' and can only use donations to address the effect rather than the cause. This is the principle issue that has been picked up in the consultation paper, which seeks to allow for multiple charitable purposes. In the current environment most charities need to address multiple social issues (purposes) to be effective.

There are currently 51 distinct DGR categories including welfare, health, education, environmental and cultural entities. Each category has its own unique set of eligibility criteria that organisations need to meet to obtain that particular DGR status. However, not every organisation is eligible for DGR status as each category is specific in its purpose. There is not a DGR category for every activity carried out in the community, which makes it difficult for some charities with a specific purpose to gain DGR status.



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***Substantive overhaul of the DGR legislation***

The Partnership supports a number of the proposals set out in the discussion paper as highlighted below. However, the changes are incremental. The Partnership advocates for a greater overhaul of the DGR legislation to amend tax laws to remove all DGR categories and replace with fewer, but broader, categories that fit with a multiple purpose framework and also reduce complexity which is one of the key issues with the current DGR legislation.

The Partnership would go further and support the creation of one general DGR category that does not limit a charities' activity to one of the 51 categories, or requiring multiple category endorsements, thus assisting charities approach an issue with a value chain or whole of community lens.

On the question of advocacy, the Partnership has not formed a definitive view. We have noted the ACNC's approach and believe that the guidance it has offered and the boundaries it has provided are a useful framework for charities that also have some advocacy element as part of their work. This approach of guiding charities to compliance rather than setting definitive measures is preferred by the Partnership in a rapidly changing environment.

This view aligns with previous investigations into the DGR framework, including the Not-for-profit Sector Tax Concession Working Group's report *Fairer, Simpler and More Effective Tax Concessions for the Not-for-Profit Sector* (May 2013), which built upon a similar recommendation in the Productivity Commission's report *Contribution of the Not-for-Profit Sector* (February 2010).

The Treasury discussion paper has picked up many of the issues that need to be addressed and which will contribute to building a transparent framework that assists build trust with donors and the wider community. There are additional issues which fall within the 'innovation' context that could further modernise and strengthen the framework to drive more strategic transformational outcomes, such as a new "business model/legal structure". A key focus for the Partnership is the exploration of social enterprise and impact investment options. Social enterprises are an emerging trend which will help build the sustainability and viability of the charitable sector in Australia. Although these issues were raised in the recent Treasury consultation on Social Impact Investment, the Partnership would like to see the issues addressed in the context of DGR reform.

Social enterprise is 'enterprise' by definition – the majority of their revenue is generated from trading. They are not generally charities although part of their DNA is always to have an impact on the communities in which they operate or to support a charity they are aligned to through profit distribution and employment opportunities for the charity's demographic. The majority of their revenue does not come from 'fundraising'. The approach taken in the discussion paper reflects a view that social enterprises should be categorised as not-for-profits and if this approach is adopted it would restrict the real value of social enterprises, i.e. helping community outcomes, innovating ways to resolve social issues, creating employment opportunities and helping charities to be sustainable by reducing their need to rely on government funding and philanthropic donors.



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Social enterprises are different to charities and should not be subject to the identical regulations as charities. All social enterprises have some form of regulation via the Corporations Act or the applicable Co-operative Law, and additional regulations should take this into account.

Modernising the DGR legislation with consideration of emerging structures will help create a future ready system.

#### ***Transparency in DGR dealings and adherence to governance standards.***

Transparency and adherence to clear equitable and reasonable standards are essential elements for a modern fit-for-purpose DGR framework. The easiest way to achieve this is to require every not-for-profit and charities to be approved as a charity with DGR endorsement to follow. This overcomes the exceptions which currently exist and brings all organisations under one umbrella (ACNC) of governance. One set of rules will make it clearer for everyone involved and improve consistent governance across the sector.

All DGRs should also qualify under the regulations as charities because the categories are similar in both Acts. As charitable status is a prerequisite of endorsement for many DGR categories, including two of the four DGR registers—the Register of Harm Prevention Charities and the Overseas Aid Gift Deduction Scheme – there is an argument to standardise this for consistency and equity.

This approach may impact on Cooperatives and Mutuals. There are currently more than 700 co-operatives that are registered charities, and approximately 150 co-operatives with DGR status. These co-operatives operate in a range of sectors including community radio, aboriginal services, education, health, care services and employment services. Co-operatives operate under a robust governance framework that is designed to protect purpose and therefore the need for further regulation of co-operatives, as charities *and/or* DGR status holders, should be carefully evaluated.

Consideration is also needed for unintended consequences. ACNC registration and reporting are relatively easy for small charities to meet, but the ACNC requirement to be an ABN registered entity may affect some regional and smaller DGRs which may not have an appropriate legal structure.

Any recommended changes should consider all potential structures as well as allowing organisations a period to transition to the new regime, similar to that adopted when the ACNC register was first initiated.

Public transparency for Public Ancillary Funds (PAFs) has also been managed, with an existing process in place for PAFs to request public confidentially under the ACNC register. As long as this provision is retained there should not be concerns with privacy balanced with appropriate oversight and governance by ACNC.

Any additional scope given to the ACNC would require additional resourcing of the ACNC, to ensure it could be undertaken effectively and achieve the desired outcomes, and is strongly encouraged by the Partnership.



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***Ensuring that DGRs understand their obligations, for example in respect of advocacy.***

We advocate for minimising burdensome red tape, as we have heard of the excessive time invested navigating regulations and processes taking resources that could be directed to achieving outcomes for communities. However we suggest careful consideration of changes to ensure negative unintended consequences are managed.

The Partnership strongly encourages a focus on charity purpose as opposed to activity. A charity may achieve its purpose via a range of activities, and purely reviewing activities may fail to consider the wider purpose for which the charity exists.

Clarity is needed on a number of issues:

- clearly and unambiguously define 'advocacy' noting the blurred line between advocacy and education
- acknowledge the likelihood that advocacy and services/program provision can often be integrally linked and challenging to delineate for the purpose of measurement, and
- note that effectively achieving positive outcomes for community can and should be linked to advocating for the needs of vulnerable groups who are not positioned to do so on their own behalf.

If data about charity advocacy activities is collected, there needs to be clear and transparent guidelines about what the data would be used for, ensuring the information cannot be 'politicised' in the case of a charity taking a stance against a controversial Government position.

We believe the annual statement is the best mechanism to collect DGR information as it is the one reporting document commonly used by charities to ACNC. The Partnership also believes that the current ACNC approach which is one of guidance and monitoring is preferred over specific percentage figures. This reflects the practical reality for charities, for example one year a charity may require a significant advocacy effort because of a specific legislative or policy change which might rightly be its focus for that year. The concept of percentages could create issues for charities achieving their purpose or fulfilling their commitment to donors.

***Complexity for approvals under the four DGR registers.***

The Partnership's preferred framework would be a common and streamlined approach to the four DGR registers, brought into the administration of ATO. ACNC would register those organisations eligible for charity status, and provide a 'one stop shop' service to charities by passing their details on to ATO for DGR endorsement. ATO would maintain registers of organisations with endorsement under each of the four DGR registers, whether the endorsement arises by virtue of the organisation's charity sub-type, a charity-like government entity, or a specific listing.

Rather than retain the numerous DGR categories, the Partnership supports the creation of one general DGR category that does not limit a charities' activities to one of the 51 categories, thus assisting charities approach an issue with a value chain or whole of community lens.



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Noting this may be challenging reform in the short term, the Partnership supports a transitional arrangement as proposed in the discussion paper, with charities able to nominate multiple DGR categories within which they would operate.

It would be critical to maintain the existing close working relationship and data sharing arrangements in place between ATO and ACNC to streamline the registration process and any ongoing reporting obligations for ACNC registered charities on each DGR register.

The Partnership would expect the appropriate subject matter experts relevant to the four registers to be consulted, however, if the relevant portfolio ministers are required to sign off and the process is not streamlined, consolidating the registers may not achieve the aim of simplification. To ensure the aim is reached, there should be adequate resources in place, along with transparent service level agreements which should be publicly reported on annually.

#### ***Complexity and red tape created by the public fund requirements.***

The Partnership supports reducing complexity and red tape created by the public fund requirements. The definition of 'responsible persons' is varied, with many rural and regional charities challenged with the strictest application of the definition. The role and definition of public officer causes a lot of confusion and the public fund concept is not well understood or administered. The Partnership supports:

- utilising a standard definition of 'responsible person' to reduce confusion about public funds
- ensuring the definition of 'responsible person' meets a benchmark consistent with community expectations i.e. extends beyond the corporations law test but which does not put unnecessary burden on small organisations especially in regional and rural areas. However, any definition should not be prohibitive and to ensure integrity of the system there should be an easy way for responsible persons to be vetted, e.g. requiring a National Police Check and/or ASIC register search for disqualification or breach of duties.
- removing the public fund requirement (such as requirement to have a standalone bank account for public funds) and allowing DGR entities to be endorsed in multiple categories, or one general DGR category.

#### ***DGRs endorsed in perpetuity, without regular and systemic review.***

The Partnership recognises that the proposed reviews are a way to protect public confidence in the charity sector. However, the following issues should be considered:

- the process should not be too onerous nor too often
- the underpinning principle should be focused on assisting charities to meet the review standards before penalising any inability to meet review standards



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- the reviews should be risk-based, prioritising
  - those charities which have been flagged as 'at risk' of non-compliance and meeting review standards being investigated further
  - larger charities or those with the greater capabilities being prioritised first

To avoid potential negative ramifications, greater clarity is sought on the purpose of any review:

- what the review will focus on
- will it be linked to impact, viability or success of the charities' work
- what criteria needs to be satisfied to retain endorsement

The Partnership notes that it will be important that ACNC and ATO be provided with sufficient resources to implement a robust, consistent and transparent approach.

***Specific listing of DGRs by Government.***

Specifically listed DGRs are currently necessary because of the inadequacy of the existing DGR framework. A general sunset rule could increase the red tape burden on organisations with a DGR specific listing, as they would need to re-apply for a specific listing, which can be a complex and time-consuming process. Any process change should reduce not increase complexity. Ideally these specific charities could be transitioned to a new reporting process to minimise complexity and cost.

The context in which specifically listed DGRs are approved may change over time and this needs to be taken into account. The onus should be on the ATO to investigate and ensure compliance based on risk. Organisations should be dis-endorsed for DGR where they fail to meet the eligibility requirements or where there is evidence of fraud or non-compliance. The Partnership believes the proposed review program will identify where DGR endorsement is no longer needed. The Partnership does not in principle support a sunset rule.

**Other issues**

There are two issues we believe should be considered as part of the DGR Reform discussions, being DGR endorsement for Community Foundations and changes to Section 50-50 of the Income Tax Assessment Act 1997.

***DGR endorsement or category for Community Foundations***

There are at least 36 community foundations in Australia, which have collectively given over \$97 million in grants to not-for-profits and charities in their communities. The current DGR categories and framework do not enable community to take philanthropy partnerships into their own hands.

Community foundations are place-based, independent, community-owned philanthropic vehicles. Community foundations are a valuable and unique form of community infrastructure, which seek to empower communities to address local challenges themselves. They act as a leader, connector,



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convenor and funder within communities and encourage civic engagement, volunteering and philanthropy.

Ideally Community Foundations would be set up as an incorporated body and be able to carry out all the activities noted above in one structure, able to receive tax deductible donations and grants from other private and public ancillary funds and carry out the work in, with and for the community benefit. This would greatly increase community philanthropy throughout urban and rural Australia.

Community foundations generally operate a 'public ancillary fund' (PuAF), an 'Item 2' deductible gift recipient which imposes considerable restrictions on their operations:

- They cannot accept donations from one of the most common forms of private foundation, PAFs, as PAFs are also an 'Item 2' deductible gift recipient, cutting them off from a significant source of philanthropic funding.
- They can only make grants to 'Item 1' DGRs, however in regional and rural areas there fewer 'Item 1' DGRs to grant to, making it difficult for community foundations to fulfil their mission and make a difference.

The Partnership advocates for a solution for Community Foundations, which is to simplify the structure to a single entity that is a deductible gift recipient (DGR) under item 1 in section 30-15 of the ITAA 97 (an item 1 DGR).

***Section 50-50 of the Income Tax Assessment Act 1997***

The discussion paper is silent on proposals for Section 50-50 Reforms. These are widely believed to place unnecessary compliance risk on charities. A more comprehensive approach to DGR reform needs to include this issue. The Section covers both not-for-profits and charities and covers quite a broad range of legal structures, e.g. associations (under state law or corporations law) which often have standard rules which they adopt which may not specifically comply with the requirements in Section 50-50. Section 50:50 should be considered as part of any DGR Reform to ensure it is practically effective in all situations.

**Conclusion**

Charities and not-for-profit organisations undertake substantial work in Australia for the benefit of our civil society. Investing in the modernisation and greater effectiveness of the enabling regulation and frameworks is necessary to ensure we maximise utilisation of limited resources. The Partnership congratulates you on taking steps to invest for better outcomes, and supports a number of the proposed actions outlined in the discussion paper.

The Partnership advocates for a greater overhaul of the DGR legislation to amend tax laws to remove all DGR categories and replace with fewer, but broader, categories that fit with a multiple purpose framework and also reduce complexity which is one of the key issues with the current DGR legislation. As stated earlier, we would go further and support the creation of one general DGR category.



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I have copied the Prime Minister and the Minister for Social Services in to this response. I am happy to expand on this response and discuss with you or your team.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Alexandra Gartmann'.

Alexandra Gartmann

Member

Prime Minister's Community Business Partnership