

## **FUNDRAISING INSTITUTE AUSTRALIA**

### **SUBMISSION TO THE DISCUSSION PAPER:**

### **NOT-FOR-PROFIT TAX CONCESSION WORKING GROUP**

### **NFP SECTOR TAX CONCESSION WORKING GROUP SECRETARIAT**

#### **About Fundraising Institute Australia (FIA)**

Established in 1968, FIA's purpose is to make the world a better place by advancing professional fundraising through promotion of standards, professional development pathways and measurable credentials so that our members achieve best practice.

The FIA has developed the Principles & Standards of Fundraising Practice as the professional fundraiser's guide to ethical, accountable and transparent fundraising. The Principles & Standards are vital to how the fundraising profession is viewed by donors, government, the community and fundraisers.

In order to achieve its mission, FIA conducts the following activities:

- Promotes and enhances education, training and professional development of fundraisers.
- Provides a resource of fundraising information.
- Is an advocate for the fundraising sector to Government, industry and the community.
- Supports and promotes the certification of fundraisers.
- Develops standards and codes of practice.
- Promotes and enhances fundraising as a profession.
- Promotes and encourages research into fundraising and philanthropic giving.

#### **EXECUTIVE SUMMARY**

FIA has had the advantage of viewing the draft submission of Community Council Australia which have assisted FIA with its response. FIA supports the comments of CCA in general.

Where FIA differs or wishes to express a particular view, it has elaborated on its responses in this paper. Where it was not appropriate for FIA to respond, it has omitted those questions.

FIA is of the view that government policy should aim at stimulating development of the not for profit sector, in particular charities (as these are FIA's main focus), rather than attempting tax reform aimed at raising further revenue for government. The not for profit sector deserves support because not only does it add high economic value to the Australian economy, but provides cost effective socially beneficial services for the public benefit which otherwise would fall to government to provide.

For this reason, FIA makes the following recommendations:

- Support the existing tax exemptions for charities in the Income Tax Assessment Act 1997 including income tax, FBT and GST;
- Support the "public benefit" test for identifying charitable purposes;
- No restriction on the kind of fundraising activities undertaken by charities, including commercial or social enterprises aimed at raising funds for a charity and which distribute all profits or surpluses to the charity operating them;
- Maintain or increase tax concessions for commercial activities of charities, provided that all profits are applied to the charity's purpose and are not distributed to members;
- Allow tax deductible gifts for Australian charities which distribute funds overseas and oppose the "in Australia" test as inconsistent with modern fundraising in a global economy.

## **OVERVIEW OF FUNDRAISING BY AUSTRALIAN CHARITIES**

Australian charities follow a fee dominant model, ie 63% of funds are privately raised, although, surprisingly, not from private philanthropy, but from fees and payments, rather than reliance on government funding (Salamon and Anheir, 1999, *The emerging sector revisited*, Baltimore, Centre for Civil Society Studies, Institute for Policy Studies, Johns Hopkins University). While the market in Australia for not-for-profit services is large, further growth is limited because of the dependence on private fundraising. As only about 30% of funding in Australia comes from government, with the remainder raised privately, further support by government will increase the not-for-profit sector's efficiency and effectiveness.

One way of doing this is by increasing the available range of Deductible Gift Recipients (DGRs). Gifts to charities have been deductible in Australia since the introduction of Commonwealth income tax legislation in 1915 (O'Connell, *The tax position of charities in*

*Australia – why does it have to be so complicated* (2008) AT Rev 17 at 21.) Treasury has estimated that the cost of providing gift deductibility was \$710 million in 2007-2008 (O’Connell, 2008, citing Treasury, *Tax Expenditure Statement 2006*, item A64). By contrast, the general level of giving in Australia is around \$11 billion (Giving Australia, *Research on Philanthropy in Australia, Summary of Findings*, 2005). Given the value of revenue from charities in Australia, this is a very modest level of subsidy, being much less than 1 per cent of all giving.

Treasury is referred to the Henry Report 2010, para B 32. Income tax concessions for NFPs are not detrimental to charities or the economy. Income tax exemption is not necessarily a concession, as implied in the Treasury paper. For example, churches, religious organisations and charities have never been subject to payment of income tax. Therefore, the tax has not been foregone or conceded; it has never been collected. Mutuality is not equivalent to tax expenditure.

Given the small cost of gift deductibility compared to the productivity of the not-for-profit sector, there is no good economic reason to reduce this level of subsidy; or waive tax deductibility; or reduce the number of DGRs. Rather, there is a solid argument for government support to be increased for a sector which is so valuable to the Australian community, both economically and socially.

FIA sets out its answers to individual questions on the following pages.

## FIA ANSWERS TO QUESTIONS

Q 1 *What criteria should be used to determine whether an entity is entitled to an income tax exemption?*

The proposal that exemptions should be limited to charities “in Australia” does not accord with the way in which large charities operate or with Australian government policy which provides aid overseas and has set guidelines for the granting of such aid and for distribution of donated funds. It is clear that Australian donors support charities which raise funds for overseas distribution. If a charity is based in Australia, donations should be tax deductible, even if they are spent overseas.

Q 2 *Are the current categories of income tax exempt entity appropriate? If not, what entities should cease to be exempt or what additional entities should be exempt?*

The current categories are appropriate.

Q 3 *Should additional special conditions apply to income tax exemptions? For example, should the public benefit test be extended to entities other than charities, or should exemption for some types of NFP be subject to different conditions than at present?*

The public benefit test is appropriate and should be maintained as it enables new categories of charitable purpose to be developed as society changes. FIA only represents fundraisers for charity and therefore cannot comment on other NFPs.

Q 4 *Does the tax system create particular impediments for large or complex NFPs?*

It is too limiting in a rapidly and continuously changing economic environment to specify what activities an NFP is allowed to conduct in pursuit of its objects, as this may cause the NFP to miss a valuable opportunity to raise funds for its purpose. It is simply common sense that an NFP may engage in practical activities to raise funds, rather than relying solely on donations, or other passive forms of fundraising such as bequests.

Q 5 *Should other types of NFPs also be able to claim a refund of franking credits?*

FIA makes no response as not applicable to FIA members.

Q 6 *Should the ability of tax exempt charities and DGRs to receive refunds for franking credits be limited?*

No. There should be no limit on refunds for franking credits as to do so may limit charities and DGRs from obtaining funding or force them to seek alternative funding that may be more difficult to obtain.

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

The ACNC will endorse charities only as DGRs. There is no need to increase the ATO's involvement with charities as this could easily lead to the creation of a dual regulatory regime, rather than the streamlined regime the ACNC is intended to be.

Some NFPs such as community organisations already are exempt from GST, FBT and income tax. The status quo for such organisations should remain. The rationale for this is that they generally do not earn particularly large incomes and therefore would not be liable to pay tax.

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

It is unclear whether the question refers to government or quasi government bodies or NFPS. In relation to incorporated associations (which are registered at State or Territory level), they are already subject to the provisions of the ITAA 1997, including current available exemptions.

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

Clubs should be treated separately from incorporated associations and societies as clubs are able to earn a large income from gaming, which is not available to associations and societies. Charitable gaming has considerable limitations upon it which restrict the revenue gained from it, especially compared to the revenue from poker machines, betting and other gaming activities allowed in clubs. Therefore, FIA supports differential income tax exemptions for clubs compared to associations and societies, which should be treated more favourably as they have more limited sources of income and revenue.

Q 11 *Should all charities be DGRs? Should some entities that are charities (for example, those for the advancement of religion, charitable child care services, and primary and secondary education) be excluded?*

Yes. All charities should be DGRs as there is no reason why some should be preferred as charities over others if they meet the guidelines. Similarly, there is no reason why certain charities ie those for the advancement of religion, charitable child care services, and primary and secondary education, should be excluded, as these are activities conducted for the public benefit.

Q 12 *Based on your response to Q11, should charities endorsed as DGRs be allowed to use DGRs funds to provide religious services, charitable child care services, and primary and secondary education?*

Yes. The real test of a charity is whether its purpose is charitable, rather than the activities it conducts. This was clearly stated by the High Court of Australia in *Commissioner of Taxation v Word Investments Ltd.* [2008] HCA 55. This case did not invent any new law but reiterated the principles behind current law on charities.

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

No behavioural distortions have been identified in the discussion paper and therefore this question is outside the scope of the discussion paper.

Q 14 *If DGR status is extended to all endorsed charities, should this reform be implemented in stages (for example, over a period of years) in line with the PC's recommendations, or should it be implemented in some other way?*

Extension of DGR status should be staged solely for the practical reason of enabling small and medium charities to improve their governance and prepare their audits in preparation for attaining DGR status.

Q 15 *Would a fixed tax offset deliver fairer outcomes? Would a fixed tax offset be more complex than the current system? Would a fixed tax offset be as effective as the current system in terms of recognising giving?*

There is no evidence that a fixed tax offset would deliver fairer incomes and it could impact adversely donations by high income earners.

Q 16 *Would having a two tiered tax offset encourage giving by higher income earners?*

No. A two tiered system would complicate compliance by charities and would not encourage high income givers, as tax deductibility is not the only reason that donors give to charities. There are other reasons such as altruistic purpose in assisting the charity's mission or benefiting society, as discussed in FIA's answers to Q 17, 19, 23 and 24.

*Q 17 What other strategies would encourage giving to DGRs, especially by high income earners?*

Research shows that donors give because they are aligned with the charity's mission, or donating gives status (especially in the case of high income earners). Therefore, efforts to improve both public confidence in charities and their status will encourage giving (Dr W Scaife et al, *Foundations for Giving*, The Australian Centre for Philanthropy, UT, Feb 2012)

*Q 18 Should testamentary giving be encouraged through tax concessions and what mechanisms could be considered to address simplicity, integrity and effectiveness issues?*

There are no death duties in Australia and therefore no benefit to an estate in giving tax concessions. The exception is property gifts, which may be subject to capital gains tax. Some consideration could be given to reducing or waiving capital gains tax on testamentary gifts of property to reduce transfer costs of properties to charities.

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

There is no evidence that charities are unable to control their own collection of donations and major gifts, or need government assistance to do so. If compliance measures are implemented, in particular relevant accounting standards, then charities should have no difficulty in accounting for the funds they collect. A clearing house linked to the ACNC Register (not ASIC or ATO) would add another layer of red tape and compliance for charities, and deprive them of control over their own funds. It would also have the effect of distancing charities from their donors, and QUT research shows that the relationship between charities and their donors is critical to the successful raising of funds for the fulfilment of charities' missions (Dr W. Scaife, *Foundations for Giving*, op cit)

*Q 20 Are there any barriers which could prohibit the wider adoption of workplace giving programs in Australia? Is there anything the Working Group could recommend to help increase workplace giving in Australia?*

Raising the threshold of tax deductible donations would affect adversely the volume of donation through workplace giving, as most such donations tend to be smaller, as they come from the workers' own incomes.

*Q 21 Do valuation requirements and costs restrict the donation of property? What could be done to improve the requirements?*

Costs of valuation and transfer of property should be tax deductible to reduce the costs of transferring property through gifts or bequests to charity.

*Q 23 Are there additional barriers relevant to increasing charitable giving by corporations and corporate foundations? Is there anything the Working Group could recommend to help increase charitable giving by corporations and corporate foundations?*

In *Foundations for Giving* (Dr W. Scaife, QUTY, op cit), the research emphasises the non financial aspect of giving as a motivator for donors. The real motivation for donors is that people give as an expression of their values and a desire to have a relationship with the organisation that has the best fit with those values. Therefore, enabling financial structures which enable donors, in particular high value donors, to achieve those goals should be given priority.

The study found that choice of structure was made by individual preference, rather than claims of tax deductibility. In particular the following was noted:

- Endowment sub-funds in trustee companies or community foundations are described as convenient for their relative ease of entry with smaller dollars, and the backup of experienced professional advice and administration.
- PAFs are favoured as a structure that offers particular financial benefits, a high level of autonomy, can honour a family and can continue through the generations with progressive family involvement.
- Other individual charitable trusts may be able to fund beyond DGR organisations or require less reporting.
- Corporate foundations are equally diverse in structure, depending on the outcomes they are seeking.



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

As stated in Q23, PAFs are favoured by high income donors for a number of reasons which encourage giving. Therefore, their structure should not be overly restrictive. In particular, the requirement that a PAF give only to a DGR can be limiting, as many trustees would like to donate funds to good causes without DGR status eg hospitals or schools or social enterprises (which are not yet well developed in Australia because of taxation and tax exemption issues).

Limitations on minor charitable activities by PAFs should be eliminated as this would give PAFs more flexibility in giving.

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

Not applicable to FIA members.

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

No. Research by The Australian Centre for Philanthropy shows that this would prevent low income donors from donating. A significant proportion of funds raised is from donations in the category \$0-\$50 Australia wide (Prof M. McGregor-Lowndes and E. Pelling, *An examination of tax deductible giving by individual Australian taxpayers 2008- 2009*, The Australian Centre for Philanthropy, QUT, 2011)

Modern fundraising techniques such as face to face fundraising and workplace giving rely for their success on large numbers of people regularly giving small amounts of money. This income would decline if it was no longer tax deductible and would affect charities' ability to plan their operations in accordance with best business practice.

Q 31 – Q 42 *FBT tax concessions*

As a policy issue, FIA supports the status quo and opposes any changes which would reduce FBT concessions. FBT concessions enable public benevolent institutions (PBIs) to attract highly qualified professional staff who may otherwise prefer to remain in the private market. PBIs tend to be the larger charities by their nature, and are required to manage and distribute

substantial revenue streams. By attracting such professionals, charities are able to conduct their operations more effectively and efficiently, which is for the public benefit.

Any unforeseen consequences of FBT concessions may be amended, but they are not sufficient reason to abolish the concessions entirely. If any changes are to be made, they should be brought in gradually so that PBIs and other organisations making use of FBT concessions can manage their revenue streams and gradually increase wages. A sudden change in the present system could increase costs to a PBI or hospital by at least 20% (anecdotal evidence from FIA members), which would have a disastrous effect on the organisation's ability to carry out its operations and retain staff.

Further, FBT tax concessions should be adjusted to keep pace with increases in inflation and the cost of living, which means that eligible employees in the NFP sector fall further behind their private enterprise counterparts. The thresholds should be increased to reflect CPI increases since their establishment.

*Q 43 Does the existing fundraising concession create uncertainty, or additional compliance burdens, for NFP entities that wish to engage in fundraising activities that fall outside of the scope of the concession?*

FIA is not aware of any such difficulties as these have not been reported by its members.

*Q 44 Would a principles-based definition of the types of fundraising activities that are input taxed reduce the compliance burden for entities that engage in fundraising?*

Yes. The purpose or principles based test is consistent with common law interpretations, and the current status quo in the Income Tax Assessment Act 1997 (Cth) as interpreted by the High Court and Federal Court in *Commissioner of Taxation v Word Investments Ltd* [2008] HCA 55, *Commissioner of Taxation v Wentworth District Capital Ltd* [2011] FCAFC 42, *Commissioner of Taxation v Co-operative Bulk Handling Ltd* [2010] FCAFC 155.

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

Yes. There is no evidence that the status quo is causing any disadvantage to government revenue and it provides assistance in particular to small and medium NFPs.

Q 47 *Would an opt in arrangement result in a reduced compliance burden for charities that would otherwise need to apply apportionment rules to supplies made for nominal consideration?*

An opt in arrangement is likely to be seen as an increased compliance burden. Supplies for nominal consideration should be GST free as little or no GST would be payable on them.

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

Not applicable subject to answer for question 47.

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

Any alternatives would be too complicated especially for small or medium charities. The GST system is well understood and catered for in accounting systems, and therefore dealing with compliance through the GST system is preferred.

Q 50 *Should the gaming, catering, entertainment and hospitality activities of NFP clubs and societies be subject to a concessional rate of tax, for income greater than a relatively high threshold, instead of being exempt?*

*Yes in relation to gaming.* This is a public policy issue. There is no reason why large scale gaming should be exempt, as it is an activity which generates a high level of revenue for minimal supervision. Catering, entertainment and hospitality should be treated differently to gaming, as they provide a benefit to the consumer, whereas gaming only provides a benefit to the organisations conducting those activities. Gaming pay outs to gamblers are far lower than revenue received from gaming. Problem gamblers find it difficult to stop gambling when they have reached their pre-determined spending limit and keep gambling to their detriment. (Productivity Commission, *Gambling Inquiry Report*, 2009) <http://www.pc.gov.au/projects/inquiry/gambling-2009/report>

Charitable gaming can be exempted, as the revenue it generates is both limited to small amounts gambled and the activities are highly regulated by State and Territory bodies (except in the Northern Territory).

*No in relation to catering, entertainment and hospitality.* There are no real public policy reasons to tax such activities, as they can be considered to be beneficial activities contributing to sustenance and leisure.

*Q 51 What would be a suitable threshold and rate of tax if such activities were to be subject to tax?*

Given the answer to Q 49, FIA does not comment.

*Q 52 Should the mutuality principle be extended to all NFP member based organisations?*

The mutuality principle should be extended for simplicity of compliance and administration.

*Q 53 Should the mutuality principle be legislated to provide that all income from dealings between entities and their members is assessable?*

No. In the case of charities, their constitutions prevent dealings between entities and their members and therefore this is not an issue. In cases where dealings are allowed, there is no public policy reason why dealings between entities and their members should be taxed. This would make the compliance burden on entities onerous and it is dubious whether any significant taxation revenue would be accrued.

*Q 54 Should a balancing adjustment be allowed for mutual clubs and societies to allow for mutual gains or mutual losses?*

Not applicable to FIA members as they are not clubs.

*Q 55 Is existing law adequate to address concerns about exploitation of the mutuality principle for tax evasion? Should a specific anti avoidance rule be introduced to allow more effective action to be taken to address such concerns?*

Not applicable to FIA members as they are not clubs.