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Submission to the Senate Community Affairs Legislation Committee regarding the *Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012*

By the Standing Committee of the Synod of the Anglican Church Diocese of Sydney

1 Introduction

(a) The name of our organisation is the Anglican Church Diocese of Sydney. This submission is made by the Standing Committee of the Synod of the Diocese.

(b) We welcome the opportunity to make further submissions concerning the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (the "Bill").

2 Summary of Recommendations

(a) We recommend that the words "or benefits" be omitted from subsections 30-18(3) and 50-50(4).

(b) We recommend that the legislation provide that where the use of money by recipient entities (whether or not the initial recipient) is to be taken into account for the purposes of subsections 30-18(3) and 50-50(4), the use should be determined by reference to what the exempt entity providing the money or property knew or should reasonably have known about its use.

(c) We recommend the Bill provide that the Australian Business Register (or public information portal of the ACNC once established) can be relied upon as conclusive evidence of whether an entity is a deductible gift recipient or tax exempt entity for the purposes of subsections 30-18(3) and 50-50(4).

(d) We recommend the reference to "conditions (if any) prescribed in the regulations for the purposes of this subsection" be omitted from subsection 50-50(5).

(e) We recommend that for the purposes of subsection 50-50(3), a definition of "substantive requirements of governing rules" be inserted along the lines of that in paragraph 1.100 of the Explanatory Memorandum (namely objects and not-for-profit clauses).

(e) We recommend that a suitable process for affording an entity an opportunity to rectify a breach of section 30-18 or 50-50, prior to disendorsement being instituted, should be included in the Bill.

(f) We recommend that proposed section 50-50(3)(b) be omitted as it is unnecessary and may be inconsistent with possible future reforms in respect of unrelated business activities.

3 Gifts and Donations

(a) We note that subsection 30-18(3) (for DGRs) and subsection 50-50(4) (for other exempt entities) require that if an exempt entity provides money, property or benefits to another entity that is not a DGR or an exempt entity (as the case may be), the use of the money by the recipient (or any other entity) be taken into account in determining whether the giving entity satisfies the requisite test about operating and pursuing its purposes in Australia. This gives rise to several matters.

Benefits

(b) The term "benefits", now included in subsections 30-18(3) and 50-50(4), has not been included in prior exposure drafts of the Bill. The explanatory memorandum does not give any indication as to why it has been included at this late stage.

(c) We are concerned about the lack of clarity concerning the scope and meaning of the term "benefits". Potentially it may extend to benefits that are not tangible which would not ordinarily be subject to the tax system. For example, an exempt entity allowing another entity with which it is affiliated to use its goodwill in promoting a project. There may also be circumstances where a mutual benefit is derived such as where an exempt entity sends its staff overseas on a short-term secondment with an entity overseas. Arguably these forms of assistance could constitute benefits. It seems to us that if a benefit takes tangible form in any material sense, that it will be in the form of either money or property and that these words are sufficient on their own to capture the intent of subsections 30-18(3) and 50-50(4).

Recommendation

(d) We recommend that the words "or benefits" be omitted from subsections 30-18(3) and 50-50(4).

No limit to enquiry

(e) Subsections 30-18 (3) and 50-50 (4) effectively impose an onus on donor entities to make enquiries about the ultimate destination of gifts they make. We note that neither subsection 30-18(3) nor subsection 50-50(4) set out any particular enquiries or other steps that must be undertaken by the giving entity to determine how the recipient entity uses the given amount. The problem is increased with the inclusion of the words "or any other entity" in brackets in those subsections. Potentially there is no limit to the enquiries the giving entity needs to make concerning its gift.

(f) We submit that this is an unreasonable compliance burden. In particular, it leaves exempt entities exposed to the possibility of disendorsement on the basis of misrepresentations by others about how its gifts will be used or where others do not apply gifts in the manner instructed by the exempt entity when making the gift.

Recommendation

(g) We recommend the Bill provide that where the use of money by recipient entities (whether or not the initial recipient) is to be taken into account for the purposes of subsections 30-18(3) and 50-50(4), the use should be determined by reference to what the exempt entity providing the money or property knew or should reasonably have known about its use.

Enquiries concerning tax status

(h) Subsections 30-18(3) and 50-50(4) will require the tax status of all recipients of donations (whether the initial recipient or subsequent) to be ascertained before any donations are made in order for the exempt entity to know whether the recipient's use of a donation outside Australia will be taken into account in determining the extent to which the exempt entity operates, and pursue its purposes, in Australia.

(i) Exempt entities need to have a definitive source of information concerning the status of recipients to which they can refer in order to satisfy themselves that the entity is exempt or has DGR status (as the case may be).

Recommendation

(j) We recommend that the legislation provide that the Australian Business Register (or public information portal of the ACNC once established) can be relied upon as conclusive evidence of whether an entity is a deductible gift recipient or tax exempt entity for the purposes of subsections 30-18(3) and 50-50(4).

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4 Disregarded amounts

(a) Subsection 50-50(5)(b) provides that use of non-deductible gifts or contributions received by an entity are to be disregarded in determining whether that entity operates and pursues its purposes in Australia.

(b) We note that subsection 50-50(5) includes a proviso that "…the entity must comply with the conditions (if any) prescribed in the regulations for the purposes of this subsection…". The explanatory memorandum lists the following conditions that are expected to be prescribed by regulation –

- the entity must demonstrate that any activities undertaken outside Australia and the use of any money or property outside Australia is effective in achieving the entity's purpose;
- the entity must comply with all Australian and foreign laws, Australia's international treaty obligations, and uphold the high reputation of Australia and its not-for-profit sector when sending money overseas; and
- the entity must show it has in place current and appropriate governance arrangements for the proper monitoring of any overseas activities undertaken by both it and any in-country partners to ensure that any money and property are being used in an proper and effective manner.

(c) The first bullet point's reference to demonstrating that the use of money or property is effective in achieving the entity's purposes is unduly subjective. We submit that a regulator is not in a position to judge whether an entity is effective or not in fulfilling its purposes, only whether it is pursuing those purposes.

(d) It is not clear how the condition contemplated in the second dot point will work in practice. Conceivably a charity would need to obtain legal advice from an overseas lawyer concerning the laws in force in the foreign jurisdiction and a lawyer specialising in international law concerning Australia's treaty obligations before it could forward any gifts or contributions overseas. The cost of compliance may mean that small-scale charities can in practice gain no benefit from the disregarded amounts provisions.

(e) The monitoring requirements in the third bullet point are also unduly subjective referring to "proper", "appropriate" and "effective" arrangements. It will be difficult for an entity to know whether its arrangements meet these requirements regardless of how careful it is in putting monitoring arrangements in place.

(f) We note that the *Income Tax Assessment Act 1997* presently contains a disregarded amounts provision that is not subject to conditions. The explanatory memorandum for the Bill does not disclose any difficulties with the present provision and to our knowledge there are none. There is therefore no apparent need to impose these further compliance burdens on entities that fund activities overseas via donations they receive from supporters from their after tax income.

Recommendations

(g) We recommend the reference to "conditions (if any) prescribed in the regulations for the purposes of this subsection" be removed from this subsection.

5 Compliance with substantive governing rules

(a) Proposed subsection 50-50(3)(a) requires compliance with "all the substantive requirements" in an entity's governing rules.

(b) There will be potential for uncertainty about which requirements are substantive requirements. Most entities will have substantive requirements in their governing rules which have little relevance to their tax status.

(c) We therefore submit that the legislation should define "substantive requirements" along the lines of paragraph 1.100 of the explanatory statement to mean those requirements "relating to an entity's object and purpose and those relating to an entity's not-for-profit" status.

(d) Further, we submit that a breach or failure of one person associated with a tax exempt organisation or an isolated instance of non-compliance by an organisation should usually not result in the immediate loss of entitlement of the organisation to income tax exemption. Unless the breach is very serious, the organisation should be given some ability to rectify the breach. As currently drafted this requirement is a continuing requirement and consequently a single breach would always be sufficient to disentitle an organisation to endorsement for its entire future.

Recommendations

(e) We recommend that a definition of "substantive requirements of governing rules" be inserted along the lines of that in paragraph 1.100 of the Explanatory Memorandum.

(e) We also recommend that a suitable process for affording an entity an opportunity to rectify a breach, prior to disendorsement being instituted, be included in the Bill.

6 Use of income and assets

(a) We note that proposed section 50-50(3)(b) has been revised to require that an entity must "use its income and assets solely to pursue the purposes for which it was established."

(b) These words would appear to prevent an entity from applying any income or assets in furtherance of incidental or ancillary purposes. Treasury's Consultation Paper on *The Definition of Charity* would seem to make clear that if there is to be a statutory definition of 'charity' then, regardless of whether the test is "exclusive charitable purpose" or "dominant charitable purpose", there will be allowance for non-charitable purposes which are ancillary or incidental to the charitable purpose or purposes, as the common law presently also allows. It would be anomalous if the definition of charity permitted a charity to have such ancillary or incidental purposes but the charity is not able to apply any resources in furtherance of those purposes.

(c) Further, it is not clear how section 50-50(3)(b) relates to the possible measures to remove tax concessions in respect of unrelated business activities of not-for-profit entities. In particular, it is not clear at this stage whether the retention of profits from an unrelated business activity of a not-for-profit entity will be regarded as a failure to use its assets and income to pursue the purposes for which it was established and hence raise the prospect of disendorsement of the whole entity – rather than the removal of tax concessions just in respect of the retained profit from its unrelated business activities.

(d) In any event, we question the need for this provision at all. In order to obtain endorsement, the Commissioner of Taxation already requires that the organisation have a non-profit clause requiring the income and assets of the organisation to be used in furtherance of its objects. Consequently, this section is unnecessary if section 50-50(3)(a) requires compliance with the objects and non-profit clause included in the governing rules of the entity.

Recommendations

(e) We recommend that proposed section 50-50(3)(b) be removed on the basis that it is unnecessary and may be inconsistent with possible future reforms in respect of unrelated business activities.

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