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Dear Sir/ Madam

CONSULTATION PAPER - 'IN AUSTRALIA' SPECIAL CONDITIONS FOR TAX CONCESSION ENTITIES' JULY 2011

Thank you for the opportunity to provide the Not-for-Profit (NFP) industry's views on the reforms proposed in the Treasury consultation paper on restating the 'in Australia' special conditions for tax concession entities released on 4 July 2011.

1. About Moore Stephens

We are writing on behalf of the Moore Stephens Australia network of eight independent firms of business advisors and chartered accountants. Moore Stephens have a real understanding of the environment in which our clients operate. We currently service a diverse range of entities within the sector and specialise in providing assurance, accounting, tax and advisory services to our NFP clients. We provide a national service offering to a number of key clients operating in the Not-for-Profit sector, including the following:

- Religious organisations
- Large charities
- Football clubs and sporting associations; and
- Universities and many TAFE colleges in Australia.

We have had a long standing commitment and involvement for the past 50 years in this sector. We have been active in recent years in providing submissions to the Government's various committees and consultations to support the sector through this reform phase.

2. General comments

We support the Government's intentions in restating the 'in Australia' special conditions for tax concession entities, to ensure the tax supported funds remain in Australia and prevent possible abuse of tax exempt status for the purposes of money laundering and terrorist financing.

3. Our Concerns

We have three main concerns in relation of the exposure draft, which are:

- the meaning of 'particular entities' and restriction on profit distribution within the proposed definition of 'not-for-profit entity'
- the strict requirement to comply with all the requirements in its governing rules
- the strict requirement for the use of income and assets **solely** to pursue the purposes for which tax exempt entity was established

3.1 Proposed Definition of 'Not-for-Profit Entity'

Our first concern with the changes in the exposure draft for the 'in Australia' requirements is the proposed definition of 'not-for-profit entity' in subsection 995-1 (1), which states:

“not-for-profit entity means an entity that:

- a) *does not carry on its activities for the purposes of profit or gain for particular entities, including its owners or member, either while it is operating or upon winding up'*
- b) *does not distribute its profits or assets to particular entities, including its owners or members, either while it is operating or upon winding up.”*

Our concern is that this definition restricts distributions to particular entities, including owners or members. In particular, the term 'particular entities' within the proposed definition, has not been defined clearly in the legislation nor the explanatory memorandum. Does 'particular entities' mean all entities? Alternatively, does it include only 'its owners or members' which have been specified in the proposed definition? The ambiguous definition gives rise to uncertainty for the meaning of 'not-for-profit entities' which may cause confusion and debate upon application.

In addition, we do not see why wholly-owned subsidiaries of tax exempt entities, where the subsidiaries have the same primary objectives as their parent entities, are not allowed to distribute to their tax exempt owners or members without losing their tax exempt status.

3.1.1 Recommendation

As one of the conditions to be a tax exempt entity is that the entity has to be a not-for-profit entity, it is vital that an entity passes the test to be a not-for-profit entity. We need a clear and precise definition to avoid any uncertainty. We would recommend that the proposed definition in subsection 995-1(1) (a) and (b) of 'not-for-profit entities' be amended to include 'unless particular entities are tax exempt entities'. This would allow distributions from tax exempt entities to be made to other tax exempt entities including their tax exempt owners or members without losing their tax exempt status.

Furthermore, the term 'particular entities' needs to be clarified to explain the specific entities that are covered within the context of the proposed definition of 'not-for-profit entities' to avoid any misunderstanding upon application.

3.2 Strict requirement to comply with all requirements in governing rules

The proposed condition in section 50-50(3)(a) requires a not-for-profit entity to:

“comply with all the requirements in its governing rules”

We consider this to be a strict and possibly onerous requirement as any breach of the governing rules would mean that a not-for-profit entity would lose its tax exempt status. Whilst in practice most not-for-profits comply with most of their governing rules most of the time there are inadvertent breaches from time to time. A not-for-profit should not lose its tax exempt status due to a minor breach of its governing rules.

3.2.1 Recommendation

In order to allow a degree of practicality, we recommend that the proposed condition in section 50-50(3)(a) should be replaced with:

*“comply **in all material respects with** the requirements in its governing rules”.*

3.3 Strict Requirement for the use of assets and income

Another concern we have is that the proposed conditions in section 50-50(3)(b), may be too strict as it requires a not-for-profit entity to:

*“use its income and assets **solely** to pursue the purposes for which it was established”*

Most of the governing documents for not-for-profit entities contain specific objectives which are supported by some broad objectives to allow different activities to be undertaken to support its core altruistic purposes. As a result, it is not clear what is meant by “solely to pursue the purposes”. Generally you would expect the purposes to be very broad so it would be relatively simple to satisfy the “solely to pursue the purposes” test. However, if the intention is for this to be a strict test then we would have some concerns with this test.

In addition, “purpose” is not defined. It is not clear what is meant by “purpose” in the context of section 50-50(3)(b). Will not-for profit entities have to make it clear what their purposes are? Will the purposes be simply taken from the objects of the governing documents or will other information and evidence be taken into consideration?

As the proposed sub section 50-50(3)(a) already has a strict requirement for a Not-for-profit entity to comply with its governing rules we can see no reason for this additional sole purpose test.

3.3.1 Recommendation

For the reasons outlined above the requirement for tax exempt entities to “use its income and assets solely to pursue the purposes” is too vague and potentially too strict. We do not see the need for the proposed condition in subsection 50-50(3)(b) and believe that it should be removed. If it is the view of Treasury that a similar condition is required to be retained then we request that Treasury provide reasons for the inclusion of this requirement and make the condition clearer so that it can be understood in practice.

If you have any queries please contact Stephen O'Flynn on (03) 8635 1800.

Yours faithfully



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