9 January 2009

The Manager
Philanthropy and Exemptions Unit
Personal and Retirement Income Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir / Madam

RE: Improving the integrity of PPF's Discussion Paper

As the Director of a Corporate Trustee of a PPF, I would like to submit my personal opinion with regard to some of the discussion points as raised in the Treasury Discussion Paper on PPF's.

The opinions expressed herein are my personal ones and do not necessarily reflect the opinions of my Co Directors of the trustee company.

Firstly I agree wholeheartedly that the ATO should take over the supervision of all PPF's. The ATO has the systems and capabilities to ensure that PPF's are run correctly and for the purpose for which they are set up and as such a strengthening of the ATO's oversight and regulatory supervisory powers would be welcomed.

The philosophy of a PPF should be to provide funding for charitable purposes in a cost effective and efficient manner over the long term.

One of the main advantages of a PPF over a general funding vehicle such as the Government is that the trustees or trustee Directors of a PPF can endeavour to apply logical and commercial decision making to their grant making and in this way try to make sure that every single dollar that is donated to charitable causes is used in a cost effective manner. Anyone that I have come across in this area is especially concerned that not a single dollar of the money that is donated to charitable causes is wasted or not used wisely.

This is an extremely important point to keep in mind as in our case all our time is donated free of charge to this task and many, many days of our time are taken up each year in investigating and reviewing possible donation recipients and a very "commercial" approach is taken to ensure that any funds donated are used wisely.

With regard to a distribution rate from a PPF, I consider that a mandatory distribution rate of 15% is too high.

I would consider that an appropriate minimum annual distribution rate of 5% of the net assets of a PPF would be appropriate. With an uncapped maximum distribution rate that could be set by the Trustees.

The CPI indexation of a PPF's asset base should also be removed as this creates undue question marks surrounding how much of the assets should be distributed each year. So in effect at June 30 each year the net assets including realised and unrealised gains would be ascertained which would provide an asset base figure for the PPF to use to then compulsorily distribute a minimum of 5% of this asset base during the next financial year.

The reason for having a 5% minimum distribution rate is very simple. The concept behind a PPF should be similar to the Government's Future Fund in that the capital donated by donor's can be effectively structured to provide additional income to charitable causes over a long period of time.

This reinforcement of the way of looking at the purpose of a PPF is also very important to consider as they should not be viewed as short term funding vehicles but as long term providers of charitable capital.

If a figure such as the 15% one itemised in point 20 of the Discussion Paper is used then there would be really no point in PPF's investing into anything other than mostly cash as the investment horizon for the investment into asset classes such as shares would be too short.

One of the overriding concerns that is prevalent through the Discussion Paper is around how the assets of the PPF are invested and to try and make sure that these assets are invested wisely and that the assets are not wasted or invested into wasting assets.

One radical idea that may go quite a way to addressing this concern is to mandate that the assets of a PPF are invested by using a central investment fund and that individual PPF's are not allowed to invest their own assets.

Once again a model similar to the Future Fund could be used or in fact PPF's assets could even become a sub set of the Future Fund or a similar type of fund.

A PPF could possibly have 80 to 90% of its assets invested into this Fund or a similar type of Fund and 10% would be left in cash for the funding of annual distributions to donee organisations.

This would ensure that costs are kept to a minimum through economies of scale and that state of the art investment principles are applied. It would save cumulatively millions of dollars in compliance costs, legal and accounting costs and ensure that the supervisory tasks to be undertaken by the ATO would be simplified incredibly.

The trustees of the PPF could then concentrate solely on assessing and investigating causes and organisations to which the funds could be donated.

It would also address the situation regarding the suitability or not of possibly questionable investments such as pieces of art, collectibles or similar which do not have a proper place in the investment universe of a PPF.

This would also address the issue of what minimum asset size that a PPF should be as the operating costs would be kept low although a $500,000 minimum size as outlined in the Discussion Paper is probably still a good minimum starting point.

The valuation issues as outlined in the Discussion Paper would also disappear if this model or a similar type of model was adopted.

Using this model would also address the issue of the capabilities of the Trustees as the Trustees' efforts would be directed solely to the task of assessing and reviewing the suitability or not of recipients.

Although this idea may on the surface appear to be rather draconian in its scope, I do not believe that that the concept would be opposed strongly by all. I could well be wrong in my assessment of this, but if Trustee duties were simplified to solely concentrate on the disbursement of donations then this would probably greatly enhance these deliberations as well.

In fact it may even be worthwhile investigating how this type of pooled, highly professional approach to asset management could be used in some form or another for the asset management of tax exempt foundations of all kinds in Australia?

As to the issue of providing contact details publicly for all PPF's I would strongly disagree with this approach.

Many PPF's operate in a totally anonymous fashion and also concentrate on particular areas of charitable endeavour.

In fact if you have ever been inundated with requests from an avalanche of charities prior to the implementation of the "Do Not Call Register" after providing donations to a single charity, you will understand that providing contact details etc. publicly could end up being incredibly time consuming for Trustees and those seeking donations.

Many Trustees have implemented a particular area of concern to which they direct their efforts and they often concentrate in a particular charitable area so it would in fact be a waste of time for many charitable organisations in contacting the Trustees along with a waste of time for the Trustees in just dealing with these enquiries.

With regard to the consultation question on page 8 of the Discussion Paper as to whether two years would be long enough for PPF's to comply with the new guidelines, this is really an unanswerable question. It would obviously depend on what form the new guidelines were to take as to how long it would take to comply.

On the penalty situation, a proportional response similar to that enforced by the ATO when supervising self managed superannuation funds would be a very good idea. The ATO is experienced in this area and has the systems and people to cope with this type of enforcement and it would be far better than the "all or none" situation at present.

As to imposing criteria around the “fit and proper person” test for a Trustee, this is a very vexed question. Many donors to, or people who have established PPF’s, do not necessarily have formal qualifications.

This should not exclude these people from acting as Trustees of a PPF as it is through their endeavours that the asset base was established originally that enabled these people to set up a PPF and they should definitely have a say in how these funds are disbursed.

The current PPF Guidelines outline that at least one be a “responsible person” as outlined in clause 2.1 in the model trust deed. This requirement is very sensible and should cover most situations of probity etc. If this is felt to maybe be inadequate then a possible solution could be for at least 50% of the Trustees to be a “responsible person”. But to make it a requirement for all Trustees to be “responsible people” would be absolutely wrong.

Another form of probity enhancement could be that the annual audit of a PPF should pick up any questionable practices of the Fund. As with SMSF’s it could become incumbent upon an auditor to look for and bring to the attention of Trustees any items that may not comply with the guidelines of a PPF.

I also do not see how limiting the number of donors to a maximum number would have any disadvantages.

On the point of donations to a PPF, why is there a restriction on a maximum contribution that can be made to a PPF under its original guidelines?

Would it not make more sense that should a donor wish to donate extra funds to a PPF that they originally established, why should they not be able to donate more money to the PPF? This extra contribution would then be added to the assets of the Fund and the proposed 5% distribution rule would then apply.

As to the final Discussion Paper question on restricting PPF investments to purely liquid assets, there are a number of situations where this could be limiting to the investment of a PPF.

Many investment strategies allow for longer term investments into illiquid assets. Using the Future Fund again as an example, the long term investment mandate for the Future Fund is to invest up to 15% of it’s assets into Alternative Assets and up to 30% into Tangible Assets. Both these classes of assets are considered “illiquid” under normal investment definitions so the Future Fund in the long term is aiming to have around 45% of it’s assets in what would be termed “illiquid assets”.

The question of how the assets of a PPF should be invested hinge around the figure that is selected for a payout ratio.

As has been demonstrated over the last eighteen months of the global financial crisis, very occasionally investment markets can have extremely negative periods of return across all asset classes.

If a PPF was invested according to normal investment principles and was then required to pay out 15% of its asset base in one year such as this year, then assets may need to be sold at exactly the wrong time to fund this disbursement.

As mentioned previously if a mandatory minimum 15% payout figure was actually adopted then the correct weighting to cash assets of a PPF may by necessity be 50% or more in order to take into account periods of extreme volatility such as we are currently experiencing. The payout figure percentage drives the investment profile of the PPF and thus drives the actual asset allocation of the PPF investments.

It is probably far too politically unpalatable for the Government to mandate that all PPF's assets are invested collectively into a large PPF Investment Fund.

However as a figure of A$1.3 Billion as the total amount invested into PPF's has been quoted, then this asset base would provide sufficient scale for the use of a model such as the Future Fund. This model would however only be useful if the view was taken that PPF's are to be used for the long term funding of donee organisations.

Indeed in a utopian situation all PPF's, tax exempt Foundations and any other non tax paying entities that have as their mandate the long term funding of donee causes, may be best invested into a model similar to the Future Fund.

As mentioned previously this would alleviate many of the questions, issues, compliance matters and queries raised in the PPF Discussion Paper and would enable Trustees to focus solely on fund disbursement.

I would be more than happy to expand upon any of the points raised above in a subsequent discussion with you.