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SUBMISSION IN RESPONSE TO DISCUSSION PAPER – TAX DEDUCTIBLE GIFT RECIPIENT REFORM OPPORTUNITIES

Executive Summary

Deductible Gift Recipient (DGR) status is highly sought after by charities as it allows them to offer tax incentives to donors, which then increases their likelihood of being gifted financial donations. However, given that DGR framework in Australia has developed in an ad hoc manner, it has become increasingly complex and many Australian charities which would benefit from DGR status are unable to reap the benefits that DGR status bestows.[1] This complexity results in eligible charities often not understanding the process and therefore not applying for DGR status meaning some communities are missing out on the expertise and experience of many organisations which do not receive the necessary funding to enable engagement with them. In line with Philanthropy Australia's views on this subject matter, it is submitted here that DGR 'taxation framework should be based around principles of simplicity, clarity, certainty and ensuring there are appropriate incentives to encourage philanthropy' and to support and encourage the growing culture of giving in Australia.[2]

The DGR framework and regulation should be comprehensively reformed to support and grow philanthropy and the Not-for-profit (NFP) sector, rather than inhibit it.[3] This paper explores four areas of potential reform, including:

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[1] Seibert, K. 2016, *DGR Status for Community Foundations: A Critical Reform to Grow Philanthropy,* https://probonoaustralia.com.au/news/2016/10/dgr-status-community-foundations-critical-reform-grow-philanthropy/.
[2] Philanthropy Australia Submission, 'Tax Deductible Gift Recipient Reform Opportunities' (Draft), p. 2.
[3] Seibert, K. 2016, *DGR Status for Community Foundations: A Critical Reform to Grow Philanthropy*, https://probonoaustralia.com.au/news/2016/10/dgr-status-community-foundations-critical-reform-grow-philanthropy/.

- ACNC registration and emerging business models;
- Sunset clauses; and
- Adaptations to the Charities Act.

Philanthropy in Australia

Philanthropists are acquiring and building wealth at earlier stages in life and expressing a strong desire to give what they can in monetary terms rather than in time and resources.[4] There is also a strong motivation to give to projects and organisations which align most strongly with a family or individual's own values. The feeling of having made a difference is a key factor in the giving decision-making process.[5] People are more inclined to give and invest money and resources in projects where they can see potential long-term solutions to significant issues within the community. This is the reason social enterprise and social impact initiatives have seen such a significant growth in recent years.

Observations have been made in the *Giving Australia: Philanthropy & Philanthropists* report that the Australian government's withdrawal of key social services and support is likely to result in a detrimental social structure, especially if not compensated by philanthropy. Reduction in public funding and an increase in community need is leading to greater competition for philanthropic investment[6] and any reforms should account for these dollars being invested where they will achieve the most effective outcome. In order to sustain and increase the rate of giving which will produce long-term positive outcomes, philanthropists must be given adequate flexibility and incentives, which include a continuance and the adjustment of tax concessions associated with giving.

Australian Philanthropy is changing, the *Giving Australia 2016 survey* suggests that regulatory conditions need to recognise the diversity of causes to which philanthropists seek to give.[7] While it has been recognised that changes in regulation and accessibility have influenced the processes and volume of giving, it was also observed that there are further opportunities to encourage giving by increasing accessibility.[8]

For example, expanding the coverage of DGR status recipients to include social enterprise and wider positive social impact projects would allow greater access to philanthropy opportunities which have the potential to create as large, if not larger positive social impact than many small charitable organisations. These organisations have organisational structures that are often not compatible with current ACNC charity registration requirements.

Frustrations have been expressed 'with the limits of existing giving structures, largely regarding the limitations of gifting tax-advantaged funds to those organisations endorsed by the ATO as DGR. Participants noted that the difficulty of using these structures to maximum effect ultimately results in less funding getting through to the desired recipients of giving'.[9] One such barrier is the fact that philanthropic structures such as Public and Private Ancillary Funds (PAFs), though becoming more

[4] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016,* p. xvi.
[5] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016,* p. 81.
[6] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016, p. 75.*
[7] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016,* p. xvi.
[8] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016.*
[9] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016,* p. 73.

common, are restricted to giving only to DGR Item 1[10] (being 'doing' DGRs) charities.[11] This restricts the giving abilities of philanthropists who are seeking to give to organisations which they feel will produce a significant positive and sustainable impact.

The changing trends in philanthropy and giving mean that in order to encourage philanthropy to continue and grow, definitions and scope of DGR categories, as well as their regulation and governance, need to adapt to reflect these trends. This includes extending DGR status to include charities with preventative aims, rather than only those which provide immediate relief (a requirement in obtaining 'Public Benevolent Institution' status, and thus being within an eligible DGR category).

Increasingly philanthropists wish to be part of long-term solutions to problems within the welfare and social sectors, not just relieving them and are therefore seeking to support causes through mechanisms such as impact investment and social enterprise models, whose aim is to support communities and groups in need in a way that is sustainable into the future with the vision of developing that community into one that is no longer in need of relief.[12] Impact investing is an emerging giving strategy in Australia and has been cited as being a continuing influence on future giving practice and processes.[13]

Social enterprises are increasingly becoming recipients of impact investment funds and they, as a business model, often focus on key factors that present day philanthropists are increasingly focusing on including:

- Financial sustainability;
- Economic and social outcomes linkages; and
- Long-term solutions to poverty, as opposed to just 'relief' of it.

Under the current DGR system, philanthropists – particularly those giving through PAFS - are unable to fund organisations with a social enterprise structure despite their focus on relief for those experiencing poverty and the future prevention of poverty arising for those individuals and communities. In the absence of comprehensive reforms the DGR framework will continue to be not fit for purpose, regardless of some positive incremental improvements as contemplated by this discussion paper.[14]

Regulatory reforms

DGRs must be an ACNC Registered Charity?

Given that charitable status is embedded in the notion of public benefit, it makes sense that DGR should be directly associated with charitable status. This view justifies the position that all DGRs

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[10] *Income Tax Assessment* Act 1997 (Cth), Subdivision 30-B, section 30.15(2).

[11] Australian Philanthropic Services *'Private Ancillary Funds – A Guide,* http://australianphilanthropicservices.com.au/wp-content/uploads/2014/05/Private-Brochure.pdf, p. 6; ACNC, '*Factsheet: Private and public ancillary funds and the ACNC',* https://www.acnc.gov.au/ACNC/FTS/Fact_Type_PAF.aspx.

[12] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016* at p. 56 notes that since 2005, greater emphasis by philanthropists has been placed on funding for impact and sustainability, which means longer term investment, including the engagement of communities in co-creating solutions to local challenges, resulting in community ownership of outcomes.

[13] Baker at al. 2016. *Philanthropy and philanthropists*. *Giving Australia 2016,* p. 29 & 84.

[14] Philanthropy Australia Submission, 'Tax Deductible Gift Recipient Reform Opportunities' (Draft), p. 3.

should be ACNC registered charities. However, given the discussion in this submission regarding the benefit of social enterprise and social impact models which do not meet the current requirements to be a registered charity, it seems necessary to expand current definitions to include these contemporary organisations into existing classifications of charities. It is recommended that the ACNC investigates a charity status registration category that covers social enterprise models in order to ensure that these emerging organisational model have the capacity to apply for DGR funding in the future if they meet the requirements of relieving or preventing poverty or disadvantage for Australian individuals, communities and families.

The ability to register with the ACNC without the need to be a charity is becoming increasingly crucial as the social enterprise models are becoming a significant vehicle for change in communities as the trend towards preventative and sustainable models of community engagement increases. These organisations would greatly benefit from the philanthropic investment that DGR status would attract as would the cohorts and communities they are serving. Often there are organisations who have expertise in particular areas and can achieve better results than current DGRs who historically have not been able to solve the problem on a systemic level. Many of these organisations are unable to gain DGR status, and these are exactly the type of organisations that philanthropists are increasingly seeking to invest in.

<u>DGR recipients need to provide relief from poverty and disadvantage?</u>

The *Charities Act* 2013 (Cth) ("**Charities Act**") states that an organisation must be an entity which is 'not for profit'[15] and 'all of the purposes of which are charitable purposes'[16], including 'advancing social or public welfare'.[17] The Charities Act further states that 'the purpose of relieving the poverty, distress or disadvantage or individuals or families'.[18] The requirement for DGRs to be registered as charities with the ACNC may be viewed as an impediment to those organisations whose structures do not fit into the current 'charity' framework, unless definitions such as the requirement to provide 'relief' is amended to include prevention.

It is a widely held view that prevention is much better than cure. Allowing any issue relating to human and environmental welfare to deteriorate to the point of needing remediation and relief is the most ineffectual way of addressing community and economic concerns. Rather, it is both socially and economically more efficient and sound to encourage more investment in models which break the cycle of intergenerational disadvantage and poverty. This is where social impact and investment organisations can be successful as they seek to resolve intractable social issues, as opposed to simply 'relieving' them. Though there are many other frameworks that focus on prevention as well as relief that would be of interest to philanthropists, such as collective impact models, these projects are also excluded under current DGR categories.

Social enterprise and impact investment organisations are capable of producing positive, future-focused and sustainable outcomes within communities, but their functions could be significantly diluted if they are not able to receive gifts and donations to fund their purposes due to the limited current definition of 'charities' and 'charitable purposes'. Allowing the extension of charity and/or DGR to such organisations would result in more giving and investment in these areas of social

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[15] *Charities Act 2013 (Cth),* section 5(a).
[16] *Charities Act 2013 (Cth),* section 5(b)(i).
[17] *Charities Act 2013 (Cth),* section 12(1)(c).
[18] *Charities Act 2013 (Cth),* section 15(1).

welfare which are becoming increasingly overlooked by government and would also put a focus on prevention of wicked social issues as opposed to relief which is often the cause of welfare or charity dependence.

DGR status is administered and overseen by a number of agencies?

Transferring administration of DGR registers from the current four different government departments (namely, Department of Foreign Affairs and Trade, Department of Social Services, Department of Environment and Energy and Department of Communications and the Arts) to the Australian Taxation Office (ATO), could very well reduce the time for an organisation to be included on a DGR register, which is currently approximately 12 months, and removing the requirement for a charitable DGR to maintain a public fund.[19] Further, it seems a sensible approach to expand the role of the ACNC to oversee and monitor any organisations which have been given DGR status.

DGR status eligibility should be reviewed?

Regular review is a necessary aspect for effective regulation and governance in any field. An Annual Information Statement is a clear and concise vehicle in which to provide relevant information about a charity and DGR organisation to donors, as well as providing routine updates to the ACNC in meeting criteria for maintaining charity and DGR status.

In addition, a standard sunset clause for any and all DGR organisations will ensure that reviews are undertaken periodically (e.g. every 5 years) and that compliance with DGR standards is being met. Currently a majority of DGRs do not have a sunset clause when they are given DGR status. This leaves organisations without obligations to report to any governing body or to keep up to date with legal and regulatory requirements to maintain that status. Requiring a regular review period would ensure that DGR status organisations remain aligned with the values and functions for which they were granted DGR status. If a sunset clause was to be introduced, it would have to be tempered with a straight-forward and easily accessible review function through the ACNC which would not increase any unnecessary red-tape. While transparency and regulation are important, it would be counter-productive and inefficient to make the review process more difficult for DGRs in terms of the resources and expense involved in undertaking exhaustive compliance reporting.

Future state of charity, philanthropy and DGR

The evolution of philanthropic sector, the NFP sector and the ever changing and increasing number of people in need of assistance means that mechanisms supporting these sectors needs to be flexible and be allowed to evolve and adapt. Philanthropists are increasingly recognising the finite nature of their abilities to give contrasted with what seems like an ever-increasing number of NFP organisations vying for their funds. This trend has meant that the philanthropic sector is adapting by looking at new ways to solve complex problems and provide relief to those currently in need or crisis. This has also driven philanthropists to recognise the need for organisations they fund to be

[19] Chiew, D., Dean, C. and Whenman, S., 2017, *Tax Deductible Gift Recipient Reform – Treasury Discussion Paper Released,* https://home.kpmg.com/au/en/home/insights/2017/07/tax-deductible-gift-recipient-reform-4-july-2017.html

financially sustainable and able to find ways of funding themselves that build decreasing dependence on single sources of funding such as the philanthropic or government sectors. The rise of the social enterprise modelled organisation is a direct reaction to the knowledge that this financial sustainability is needed to create long term outcomes coupled with the increasingly accepted principle that social and economic benefit, can and should, go hand in hand. It is therefore no surprise that philanthropists are increasingly interested in supporting or incubating these types of organisations when they are focused on target areas that match their interest.

Adapting the current framework around charities and DGR status to allow more investment in diverse organisations and prevention focused work, allows these organisations not only to build the capacity of the social sector to relieve the suffering and disadvantage of individuals, families and communities now, but also to prevent further suffering in the future and ultimately reduce the reliance on the welfare sector from both a NFP and government perspective.

References:

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2. Chiew, D., Dean, C. and Whenman, S., 2017, *Tax Deductible Gift Recipient Reform – Treasury Discussion Paper Released,* https://home.kpmg.com/au/en/home/insights/2017/07/tax-deductible-gift-recipient-reform-4-july-2017.html.

3. Philanthropy Australia Submission to Treasury Discussion Paper (Draft), '*Tax Deductible Gift Recipient Reform Opportunities'*, Philanthropy Australia.

4. Seibert, K. 2016, *DGR Status for Community Foundations: A Critical Reform to Grow Philanthropy*, https://probonoaustralia.com.au/news/2016/10/dgr-status-community-foundations-critical-reform-grow-philanthropy/.